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Supreme Court of the United States

OCTOBER TERM, 1957

No. 395

UNITED STATES OF AMERICA, PETITIONER

vs.

MOLLY G. BESS

&

No. 410

MOLLY G. BESS, PETITIONER

vs.

UNITED STATES OF AMERICA

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 395, Petition for certiorari filed August 22, 1957
No. 410, Petition for certiorari filed August 29, 1957
Certiorari granted October 28, 1957

SUPREME COURT OF THE UNITED STATES

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UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Docket No. 12,026

UNITED STATES OF AMERICA, *Plaintiff-Appellee*,

v.

MOLLY G. BESS, *Defendant-Appellant*

Appendix for Appellant's Brief—Filed September 7, 1956

1 IN UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY —

Docket Entries

DOCKET ENTRIES

1952

Dec. 22—Complaint filed.
Dec. 22—Summons issued.
Dec. 22—Notice of allocation of case to Trenton filed.

1953

Jan. 7—Summons returned served on 12/31/52 filed.

Jan. 12—Answer filed.

Sept. 7—Pre-trial conference.
To be tried week of Nov. 17, 1953 (Forman)

Oct. 20—Admissions of fact under Rule 36 (service acknowledged) filed.

Oct. 20—Answers to interrogatories (service acknowledged) filed.

1955

Jan. 13—Trial moved before Chief Judge Forman *without Jury.*
Facts stipulated.
Case submitted on question of law involved.
Memorandum to be submitted.
Decision reserved.

Jan. 24—Transcript re Argument by Mr. Oppenheim filed.

Aug. 2—Notice of Assignment of Case to Judge Forman filed.

Sept. 7—Opinion filed (Forman).

Oct. 26—Notice of settlement of judgment filed.

Oct. 27—Affidavit of mailing notice of settlement filed.

Nov. 7—Ordered hearing on proposed judgment.
Adjourned to 11/21/55 (Forman).

Nov. 21—Hearing on proposed judgment before Chief Judge Forman.
Judgment to be submitted.

 1956

May 22—Order for Judgment in favor of the Plaintiff, United States of America and *vs.* the Defendant, Molly G. Bess, in the sum of $11,657.30 with costs, filed 5/21/56 (Forman).
Notice mailed.

May 22—Statement of Plaintiff's costs taxed at $46.20 filed.

May 22—Stipulation of facts filed 1/13/55 (Exhibit No. P-1).

July 16—Notice of Appeal, filed.

July 16—$250.00 in cash deposited in Registry in lieu of bond.

July 16—Copies of Notice of Appeal mailed to United States Attorney and to Clerk U. S. Court of Appeals.

IN UNITED STATES DISTRICT COURT

Stipulation—January 13, 1955

It is hereby stipulated by and between the respective undersigned attorneys representing each party to this action that the following facts shall be deemed to be true, subject however to the right of either party to offer in evidence any additional facts not in conflict therewith, and with the further understanding that counsel for each party reserves the right to object to the admissibility in evidence of the facts herein stipulated on the ground of immateriality or irrelevance.

1. This action has been authorized by the Commissioner of Internal Revenue of the United States Treasury Department and is brought under the direction of the Attorney General of the United States.

2. Defendant, Molly G. Bess, resides in Deal, Monmouth County, New Jersey.

3. Herman Bess, the husband of defendant, died June 29, 1950, a resident of New Jersey.

4. During the years involved, namely, 1945, 1946 and 1947, the decedent was a sales director of various commercial radio stations.

5. On March 15, 1946, Bess filed his income tax return for 1945, reporting thereon tax due in the sum of $11,101.88, and claiming a refund of tax in the sum of $10,218.16, which later sum was refunded to him by the Commissioner of Internal Revenue, with interest of $165.03 on August 21, 1946. Thereafter, on June 17, 1948, Bess signed a Form 870 consenting to the assessment of additional income tax for the year 1945, in the sum of $10,119.31, plus interest, following an audit of his return by a revenue agent. On July 30, 1948, the Commissioner assessed for the year 1945, the total sum of $11,514, composed of $10,119.31 additional income tax, plus $1,421.69 interest thereon. Notice and demand was made on July 30, 1948, and a second notice and demand on August 9, 1948. By virtue of periodic payments made by Bess until his death, the outstanding balance was reduced to $4,713.59. Thereafter, pursuant to an order entered on November 21, 1952, in the Monmouth County Court, the defendant, as executrix, paid to the Collector of Internal Revenue, the sum of $554.28 which sum was applied by the Collector against the unpaid balance for 1945, leaving $4,159.31, plus interest due and unpaid.

6. On March 15, 1947, Bess filed his income tax return for 1946, reporting thereon tax due in the sum of $10,710.40, and claiming a refund of tax in the sum of $3,254.69, which latter sum was refunded to him by the Commissioner of Internal Revenue, with interest of $36.83 on June 19, 1947. Thereafter, on June 17, 1948, Bess signed a Form 870 consenting to the assessment of additional income tax for the year 1946, in the sum of $3,507.03, plus interest, following an audit of his return by a revenue agent. On July 30, 1948, the Commissioner assessed, for the year 1946, the tota lsum of $3,789.32, composed of $3,507.03 additional income tax, plus $282.29 interest thereon. Notice and demand was made on July 30, 1948, and a second notice and demand on August 9, 1948. No part of the sum of $3,789.32 has been paid.

7. A true and correct photostatic copy of the Commissioner's assessment list, covering the years 1945 and 1946 is attached hereto, made a part hereof and marked "Exhibit A".

8. On or about March 15, 1948, Bess filed his income tax return for 1947. Thereafter, on August 24, 1950, the Commissioner assessed for the year 1947, the total sum of $925.94, composed of $813.22 additional income tax, plus $112.72 interest thereon. Notice and demand was made on September 8, 1950. No part of the sum of $925.94 has been paid.

9. The assessment referred to in paragraph 8 was transferred from the Third District of New York to the Fifth District of New Jersey on the January 1951 Assessment List. A true and correct photostatic copy of the Commissioner's assessment list covering the year 1947, is attached hereto, made a part hereof and marked "Exhibit B".

10. On August 1, 1950, the Collector of Internal Revenue filed proofs of claim with the defendant, as executrix of the estate of Herman Bess, for the sums of $4,713.59 and $3,789.32, being unpaid income taxes for 1945 and 1946, respectively. On January 19, 1951, a proof of claim was likewise filed in the sum of $925.94 for unpaid taxes for 1947. Proofs of claim were also filed in the sums of $1,411.19 and $2,579.52, totalling $3,990.71, for unpaid income taxes for 1948 and 1949.

11. On July 19, 1952, the defendant as executrix, submitted a Report of Claims to the Monmouth County Court, Probate Division, and listed thereon as presently due unpaid federal income taxes for the years 1945 through 1949. That report set forth claims against the estate in the total sum of $22,081.06 and, upon the basis of an inventory and appraisement, a personal estate of $6,973.85.

12. Pursuant to due notice given by the defendant, as executrix, on July 17, 1952, the estate of Herman Bess was adjudged insolvent by the Monmouth County District Court, Probate Division.

13. The defendant, as executrix, allowed all the claims filed by the Collector of Internal Revenue and thereafter paid the sum of $3,990.71 on account of unpaid taxes for 1948 and 1949 to the Collector of Internal Revenue out of the assets of the estate.

14. The final account filed by the defendant as executrix listed the following expenditures out of the total personal estate of $6,973.85:

Funeral expenses	$ 682.50
Administrative expenses	210.36
Counsel fees	1,500.00
Federal income taxes for 1948 and 1949	3,990.71
Total	$6,383.57

6 On November 21, 1952, the Monmouth County District Court ordered all the remaining funds in the estate, totalling $554.28, be paid to the Collector of Internal Revenue. This sum was applied by the Collector as set forth in paragraph 5 above.

15. On or about October 1, 1951, defendant as executrix filed with the Collector of Internal Revenue for the First District of New Jersey, an estate tax return and, for the purpose of the estate tax laws, disclosed thereon a total gross estate of $122,476.96 and no estate tax payable.

16. Upon the estate tax return, a deduction for debts of the decedent in the sum of $30,480.40 was claimed and allowed. Included in that sum were the sums of (1) $9,428.85, (2) $1,411.19 and (3) $2,579.52 representing unpaid income tax and interest for the years (1) 1945, 1946 and 1947, (2) 1948 and (3) 1949.

17. At the time of his death, Bess and the defendant had the following property in their joint names:

Checking account, Chase National Bank, New York City	$ 587.15
Real estate (equity)	52,054.48
Cadillac automobile	2,600.00

18. At the time of his death, Bess carried insurance upon his life in the total amount of $85,906, distributed among nine separate policies with five different insurers.

19. Upon one of the nine policies (issued by Prudential Insurance Company of America, Policy No. 8225731) in the face amount of $5,000, his estate was; on June

29, 1950, the named beneficiary and received thereunder proceeds in the sum of $3,834.43, by virtue of an
7 outstanding policy loan plus interest of $1,175.12, which sum was distributed by defendant as executrix and is not in controversy here.

20. Upon the remaining eight policies of insurance, the defendant, as wife of the insured, was, on June 29, 1950, the named beneficiary and received thereunder as proceeds the total sum of $63,576.95.

21. The eight policies of life insurance upon which defendant, as wife of the insured, was the named beneficiary were as follows:

	Insurer	Policy No.	Face Am't.	Date of Issue	Type of Policy	Proceeds
No. 1	John Hancock Mutual Life Ins. Co.	2700416	$32,000	9-26-35	whole life	$25,033.38
No. 2	John Hancock Mutual Life Ins. Co.	2884650	1,000	11- 1-36	45 pay life	1,071.87
No. 3	Metropolitan Life Ins. Co.	8918803A	5,000	2-14-34	whole life	3,834.91
No. 4	Prudential Insurance Co. of America	8790470	10,000	2-5 -35	modified whole life	8,785.32
No. 5	Prudential Insurance Co. of America	8790471	10,000	2-5 -35	modified whole life	8,785.32
No. 6	Prudential Insurance Co. of America	9768742	10,000	4-26-37	20 yr. endowment	5,406.22
No. 7	State Mutual Life Assurance Co.	445,636	10,406	10-12-35	whole life	8,159.93
No. 8	Aetna Life Ins. Co.	GW 31599	2,500	6-19-50	group life	2,500.00

22. On Policy No. 1, Bess had the right to borrow upon the security of the policy against the cash surrender value, or surrender the policy for cash; he had expressly reserved the right to change the beneficiary and had in fact exercised that right twice in 1945; he had the right of assignment. On June 29, 1950, the cash surrender value of the policy was by virtue of outstanding policy loans,
8 $1,169.70. A photostatic copy of the policy is attached hereto, made a part hereof and marked "Exhibit C".

23. On Policy No. 2, Bess had the right to borrow upon the security of the policy against the cash surrender value, or surrender the policy for cash; he had expressly reserved the right to change the beneficiary but did not exercise that right; he had the right of assignment. On June 29, 1950, the cash surrender value of the policy was by virtue of outstanding policy loans, $262.34. A photostatic copy of this policy is attached hereto, made a part hereof and marked "Exhibit D".

24. On Policy No. 3, Bess had the right to borrow upon the security of the policy against the cash surrender value and had exercised that right on several occasions, so that on June 29, 1950, policy loans and interest thereon aggregated $1,581.09; the cash surrender value by nature of the outstanding loans upon the date of death was only $187.45; he had expressly reserved the right to change the beneficiary but had not exercised that right; he had the right of assignment. A photostatic copy of the policy is attached hereto, made a part hereof and marked "Exhibit E".

25. On Policy Nos. 4 and 5, Bess had the right to borrow upon the security of the policy against the cash surrender value and had exercised that right so that on June 29, 1950, identical policy loans and interest thereon against each policy aggregated $1,253.28; under the terms of the policies he had the right to assign all his rights, benefits and advantages and exercised that right on February 5, 1935, the date of issue, in favor of Bess & Schillin, Inc., its successors or assigns and on April 13, 1938, at the request of the assignee, ownership of the policies was transferred to the insured. Bess had expressly reserved the right to change the beneficiary and on March 28, 1938, had exercised that right on each policy in
9 favor of the defendant, if living, otherwise his executors, administrators or assigns. On June 29, 1950, the cash surrender value of each policy was, by virtue of outstanding policy loans, $171.72. Photostatic copies of the policies are attached hereto, made a part hereof and marked "Exhibit F" and "Exhibit G".

26. On Policy No. 6, Bess had the right to borrow upon the security of the policy against the cash surrender value and had exercised that right so that on June

29, 1950, a policy loan and interest thereon aggregated $4,601.78; he had expressly reserved the right to change the beneficiary but had never exercised that right; he had the right of assignment. The cash surrender value on June 29, 1950, was, by virtue of outstanding policy loans, $933.22. A photostatic copy of this policy is attached hereto, made a part hereof and marked "Exhibit H".

27. On Policy No. 7, Herman Bess had the right to borrow upon the security of the policy against the cash surrender value and had exercised that right so that on June 29, 1950, a policy loan and interest thereof aggregated $2,246.07; he had the right to assign his rights under the policy and had, expressly reserved the right to change the beneficiary. On March 23, 1945, he changed the beneficiary from his wife to his estate, and assigned his right under the policy to The Merchants Trust Co., Red Bank, New Jersey. On April 3, 1945, he renominated his wife beneficiary. On May 6, 1946, the assignee discharged the assignment. On June 29, 1950, the cash surrender value, due to the policy loan outstanding was only $466.38. Attached hereto, made a part hereof and marked "Exhibit I" are (1) copies of letters dated October 7, 1953, and November 6, 1953, from the insurer stating that all but the face of the contract had been destroyed but setting forth the rights under the policy and the time and manner of their exercise, and (2) a photostatic copy of the face of the policy.

28. On Policy No. 8, which was group insurance, Herman Bess had only the right to change the beneficiary.

29. By reason of the death of Herman Bess, the defendant individually, as beneficiary of the policies described in paragraph 21 of this stipulation, became entitled to be paid according to their terms and has in fact received a total sum of $69,576.95 from the named insurance companies.

30. All the policies referred to in paragraph 21 of this stipulation were owned by Herman Bess who paid all the premiums until his death out of his own funds. At no time when any premium was so paid was he insolvent.

31. At no time prior to the institution of this action did the Commissioner of Internal Revenue propose a transferee assessment against defendant under the provisions of Section 311 of the Internal Revenue Code of 1939.

32. The total cash surrender value at the date of death of all the policies referred to in paragraph 21 of this stipulation was $3,362.53.

For the plaintiff:

RAYMOND DEL TUFO, JR.
United States Attorney
Newark 1, New Jersey

By: H. EUGENE HEINE, JR.
Special Assistant to the Attorney General
Washington, D. C.

For the Defendant:

DANIEL OPPENHEIM
17 Academy Street
Newark 2, New Jersey

Dated: Jan. 13, 1955

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11 IN UNITED STATES DISTRICT COURT

(Reported in 134 F. Supp. 467.)

Appearances:

RAYMOND DEL TUFO, JR., United States Attorney, by GEORGE H. BARLOW, Assistant U. S. Attorney, Attorney of Plaintiff.

H. BRIAN HOLLAND, Assistant Attorney General, ANDREW D. SHARPE, H. EUGENE HEINE, JR., Special Assistants to the Attorney General, of Counsel.
DANIEL OPPENHEIM, Attorney of Defendant.

Opinion—Filed September 7, 1955

FORMAN, C. J.:

The complaint in this case alleges that the defendant, Molly G. Bess, owes the plaintiff, the United States, for

income taxes due from her deceased husband in the aggregate of $9,428.84.

The facts are stipulated.

Herman Bess, a resident of New Jersey, died on June 29, 1950, leaving the defendant, his widow, a resident of Deal, Monmouth County, New Jersey, surviving him. On July 17, 1952 his estate was adjudged insolvent by the Monmouth County Court, Probate Division. Claims were filed by the Government for the years, in the amounts, and upon which payments were ordered to be made as follows:

12

Year	Amount	Payment Pursuant to Order of Court
1945	$ 4,713.59	$ 554.28
1946	3,789.32	
1947	925.94	
1948	1,411.19	
1949	2,579.52	3,990.71
Total	$13,419.56	4,544.99
Balance due		$8,874.57[1]

Interest on the above amounts was also claimed. It was further stipulated that Mrs. Bess succeeded to approximately $55,000 of property held in the joint names of herself and her husband;[2] that she was the named beneficiary in eight policies of insurance on the life of her husband from which she received a total of $63,576.95; that on seven of the policies the deceased had had the right to borrow against the cash surrender value, to change the beneficiary, and to assign the policies; that he did change the beneficiary on several of the policies; that the eighth policy was in group insurance and that under it he had only the right to change the beneficiary; that

(1) The demand in the complaint fails to reflect the payment of $554.28, applied to the year 1945 as stipulated.

(2) The Government makes no attempt to reach property held jointly by husband and wife. See *Irvine* v. *Helvering*, 99 F. 2d 265 (8th Cir., 1938).

the deceased paid all of the premiums on the policies and that he was solvent at the time he made such payments and that the cash surrender value of the policies at the date of his death was $3,362.53.

No facts were left disputed and the case poses only questions of law. It is the proceeds received by Mrs. Bess which the Government is now trying to reach
13 on the theory that the defendant is a "transferee" under §311 of the 1939 Code (now §6901 of the 1954 Code), 26 U.S.C. §311:

"§311. Transferred assets

"(a) Methods of collection. The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) Transferees. The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter."

* * * * * * * * * *

"(f) Definition of 'transferee'. As used in this section, the term 'transferee' includes heir, legatee, devisee, and distributee."

It is the theory of the Government that Mrs. Bess is a "transferee" of "property of a taxpayer" by virtue of having been beneficiary of his life insurance and that she is under a "liability, at law or in equity . . . in respect of the tax."

Implicit in this theory of the case is that the life insurance proceeds received by Mrs. Bess were property of the deceased taxpayer transferred to her burdened with

a liability for his tax delinquency. The Govern-
14 ment concedes, however, that several recent cases in the Court of Appeals have been decided to the contrary. *United States* v. *Truax*, 223 F. 2d 229 (5th Cir. 1955); *United States* v. *New*, 217 F. 2d 166 (7th Cir. 1954); *Rowen* v. *Commissioner*, 215 F. 2d 641 (2nd Cir. 1954); *Tyson* v. *Commissioner*, 212 F. 2d 16 (6th Cir. 1954).[3] Each of these cases distinguishes, or differs from *Pearlman* v. *Commissioner*, 153 F. 2d 560 (3rd Cir. 1946), upon which the Government places heavy reliance.

Rowen v. *Commissioner, supra,* is representative of this problem. There mutliple beneficiaries of a decedent's life insurance policies contested the Commissioner's transferee assessment against them. It was held that since life insurance proceeds were not "property" of the insured even though he had reserved the right to change beneficiaries, there was no transfer of property of a taxpayer and therefore as to the proceeds there could be no transferee liability on the part of the beneficiaries. The court held otherwise as to the cash surrender value, deciding that during the lifetime of the taxpayer the cash value represented property which upon his death merged with the proceeds and was thus transferred to the beneficiaries. But even though the beneficiaries were held to be "transferee(s) of property of a taxpayer" in the amount of the cash surrender value, there was no liability "at law or in equity . . . in respect of the tax "because the Government's rights as a creditor were to be governed by local law and under the applicable New York statutes
15 the entire proceeds of life insurance, including that representing cash surrender value, were beyond the power of creditors to reach.

But the Court of Appeals of this circuit treated such tax liability from a different viewpoint in the case of *Pearlman* v. *Commissioner, supra.* The facts in that case were not materially different from those here and in Rowen,

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(3) None of these cases gives any reason to doubt the holding of *Kieferdorf* v. *Commissioner*, 142 F. 2d 723 (9th Cir., 1944), that transferee liability may be successfully pressed against a decedent's heirs where they are in receipt of life insurance proceeds paid first to the estate as beneficiary, and then distributed to them. In fact, *Rowen* v. *Commissioner*, 215 F. 2d 641 (2nd Cir., 1954), approves the *Kieferdorf* result at pp. 645-646.

except in one particular—there the decedent had paid premiums while insolvent whereas the Government and Mrs. Bess have stipulated that Herman Bess paid all premiums while solvent. This difference was thought controlling in *Tyson* v. *Commissioner*, *supra*, which distinguished the *Pearlman* case on this ground. But although the prior insolvency of the decedent was mentioned in *Pearlman* no particular significance is attached to it in the opinion. Pearlman seems rather to be laying down a broad policy of transferee tax liability wherever life insurance proceeds are distributed to beneficiaries named by an insured who dies owing the Government for back income taxes and who had reserved the right in the policies to change the beneficiary.

> "On principle the question seems to us clearly one to be answered without reference to state law limitations. It would not be disputed that, in general, the imposition and collection of federal income tax is a federal function. One of the questions arising from such an undertaking is the determination of when B is to be liable to pay a tax assessed against A. The Congress could, no doubt, have left this question to be variously determined by the laws of the respective states if it had so desired. But in the absence of a clearly expressed intention to do so, we should not infer it, for such variation does not fit into a uniformly applied system of federal taxation.
>
> The administration of its taxing laws is as
> 16 clearly a function of the federal government as the making of contracts, and the issuing of checks and warrants in payment of its obligations, matters in which the Supreme Court has recently held that the state law does not control. Clearfield Trust Co. *v.* United States, 1943, 318 U. S. 363, 63 S. Ct. 573, 87 L. Ed. 838; United States *v.* County of Allegheny, 1944, 322 U. S. 174, 64 S. Ct. 908, 88 L. Ed. 1209; National Metropolitan Bank *v.* United States, 1945, 323 U. S. 454, 65 S. Ct. 354.
>
> "Once the problem is removed from state statutes and decisions there is no question made of the lia-

bility of this taxpayer as transferee. . . ." 153 F. 2d at p. 562.

Thus, it is easily seen that Pearlman leaves no room for the application of the New Jersey statute[4] protecting life insurance beneficiaries from their insured's indebtedness as, it is urged, is the case with this defendant. The decision in the *Pearlman* case is controlling here.[5]

The defendant further objects that the plaintiff has failed to fulfill statutory requirements contained in §311(a) of the Internal Revenue Code so as to impress her with any liability for the income tax owed by her deceased husband. She argues that any alleged claim against
17 her as a transferee must be assessed and collected in the same manner as in the case of a deficiency on a tax. Section 272(a)(1) prescribes, she contends, the administrative procedure to be followed by the plaintiff in order that liability may be established against a transferee of the nature of which plaintiff claims her to be. Since no procedure was followed by the plaintiff to satisfy the statutory requirements she submits that she cannot in this suit be adjudged responsible for the said taxes and that it should be dismissed against her. She further contends that since the plaintiff failed to follow the statutory procedure outlined it can be regarded only as an ordinary creditor of the deceased taxpayer and in order to recover from her the plaintiff must plead and prove that she was the recipient of a fraudulent conveyance of the proceeds of the life insurance policies under N. J. R. S. 17:34-28 which, she alleges, insulates her rights as a beneficiary of an insurance policy from plaintiff's reach.

The statutory procedure to which the defendant refers is not exclusive and the plaintiff may endeavor to enforce

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(4) N. J. R. S. 17:34-28.

(5) The *Pearlman case* has been construed broadly and followed by a number of district courts and the tax court, although some of these cases have been reversed. A representative group follows: *United States* v. *New*, 123 F. Supp. 312 (N. D. Ill., 1954), reversed 217 F. 2d 166 (7th Cir., 1954); *United States* v. *Goddard*, 111 F. Supp. 607 (W. D. N. Y., 1952); *Aura Grimes Bales*, 22 T. C. 355 (1954); *Ruth Halle Rowen*, 18 T. C. 874 (1952), reversed 215 F. 2d 641 (2nd Cir., 1954); *Christine D. Muller*, 10 T. C. 678 (1948). See also Pyle, Liability of Insurance Proceeds for Unpaid Income Taxes of Decedents, 31 Taxes 183, 188-189 (1953).

collection of its taxes by actions at law or in equity. *Phillips* v. *Commissioner*, 283 U. S. 583 (1931); *Leighton* v. *United States*, 289 U. S. 506 (1933).

Judgment for the plaintiff will be entered in the amount of $8,874.57.

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18 IN UNITED STATES DISTRICT COURT

Order for Judgment—Filed May 5, 1956

This cause came on to be heard by the Court sitting without a jury on January 13, 1955, and the Court having considered all the evidence and the oral arguments of counsel and briefs submitted by the parties and being fully advised in the premises, it is hereby Ordered, Adjudged and Decreed that plaintiff have and recover from defendant $8,874.57 together with interest of $697.91 (being interest on $4,159.31 from November 21, 1952 to September 7, 1955) and interest of $1,804.91 (being interest on $3,789.32 from July 30, 1948 to September 7, 1955) and interest of $279.91 (being interest on $925.94 from August 24, 1950 to September 7, 1955), or a total of principal and interest of $11,657.30, and that plaintiff have execution therefor.

Date: May 15, 1956

s/ FORMAN,
Chief Judge,
United States District Court.

Approved as to form Only:

s/ DANIEL OPPENHEIM,
Attorney for Defendant.

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19 No. 12,026

Stipulation and Order Extending Time to File Brief and Appendix—October 10, 1956

(omitted in printing)

23

Stipulation and Order Extending Time to File Reply Brief—October 31, 1956

(Omitted in printing)

* * * * * * * * * *

27 IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

UNITED STATES OF AMERICA

v.

MOLLY G. BESS, APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Argued December 4, 1956

Before BIGGS, *Chief Judge*, KALODNER, *Circuit Judge*, and KRAFT, *District Judge*.

Opinion of the Court—Filed March 28, 1957

BY BIGGS, *Chief Judge*.

The court below gave judgment in favor of the United States against the defendant, Molly G. Bess, widow of Herman Bess, on the theory that under Section 311 of the 1939 Code, 26 USCA (I.R.C. 1939) § 311, the defendant was a transferee of property of a taxpayer, her husband, who owed the government delinquent income taxes.

The facts are not in dispute. The defendant's husband died on June 29, 1950. At the time of his death there were in force eight insurance policies on his life. Seven of the policies were issued during 1934, 1935, 1936, and 1937. The eighth, a group insurance policy with no cash value, was issued June 19, 1950. Herman Bess had the right to change the beneficiary of the policies and also had the right to borrow upon the security of the cash surrender

value of the seven policies described first herein.
28 The defendant was named as beneficiary when the policies were issued to Herman Bess, and, except for temporary changes with respect to two policies,[1] the defendant remained the beneficiary. The government and the defendant have assumed, without dispute, that Herman Bess was solvent when the policies were issued, and have stipulated that he was solvent when the premiums were paid. The total cash surrender or loan value of all the policies was $3,362.53 at the time of Bess's death. The defendant received $63,576.95 as the total proceeds of the eight policies.

On July 17, 1952, more than two years after his death, the estate of Herman Bess was adjudged insolvent. Part payment has been made on the claims of the United States for income taxes owed by Herman Bess, but a balance of $8,874.57 remains unpaid. The United States instituted suit against the defendant for that amount plus interest from the date of assessment and was awarded judgment in the sum of $11,657.30. 134 F. Supp. 467 (D.N.J. 1955). Mrs. Bess has appealed.

The statute on which the alleged liability of the defendant is bottomed is Section 311 of the 1939 Internal Revenue Code, 26 USCA (I.R.C. 1939) § 311, set out in the margin.[2]

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[1] In one policy the beneficiary was changed from the defendant to the insured's estate on April 4, 1945, and on the same day the defendant was redesignated as the beneficiary; in another policy the beneficiary was changed from the defendant to the insured's estate on March 23, 1945, and on April 3, 1945 the defendant was redesignated as the beneficiary.

[2] Section 311 provides in pertinent part: "Transferred assets (a) Method of collection. The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) Transferees. The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter.

"(f) Definition of 'transferee'. As used in this section, the term 'transferee' includes heir, legatee, devisee, and distributee."

It is the universal view that the statute created no new substantive rights and liabilities and that the only liabilies to be enforced thereunder are those existing in law or in equity when the enforcement proceeding is begun. Pearlman v. Commissioner, 153 F. 2d 560, 561-2 (3 Cir. 1946), and Rowen v. Commissioner, 215 F. 2d 641, 643 (2 Cir. 1954). Herman Bess was domiciled in New Jersey up to his death. His widow's domicil remains there. In Pearlman v. Commissioner, *supra*, at p 562, we stated that "On principle the question [as to the existence or non-existence of liability on the part of the widow] seems to us clearly to be one to be answered without reference to state law limitations." We also said, since we had before us a husband domiciled in Pennsylvania until his death with his wife's domicil remaining there, that "Whether the reliance is placed on general law as declared by federal courts, or on Pennsylvania law, we think the conclusion of the Tax Court must stand." We may perhaps remark here, without cynicism, that a declaration on principle is not necessarily a declaration of law, but we went on to say that we preferred to rest the decision on the wider ground that since the e was a federal tax question to be decided it should be decided on general law as laid down by the Federal courts and not be subject to the limitation in the law of any State. We adhere to our former ruling but since this case may reach the reviewing Court, other Courts of Appeals having reached the contrary conclusion, Rowen v. Commissioner, *supra*, and the authorities cited therein, 215 F. 2d at 648-9, we have set out what we believe to be the status of Mrs. Bess under the law of New Jersey, were that that law applicable; in *footnote 3 below*. Cf. Poe v. Seaborn, 282 U.S. 101 (1930),

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[3] As to the law of New Jersey the applicable sections are New Jersey R.S. 17:34-28 and 17:34-29; NJSA 17:34-28 and NJSA 17:34-29. Section 29 provides that eve . policy of life insurance made payable to or issued for the benefit of a married woman, or after its issue assigned or in any way made payable to a married woman, whether by her husband or by any other person, shall "inure to her separate use and benefit . . ." according to its terms unless premiums were paid in fraud of creditors as set out in Section 28. There can be no doubt that in the absence of fraud on creditors in the payment of premiums or assignment of the beneficial interest to some person other than to the wife, the wife's interest in the proceeds of a policy has a status described by the law of New Jersey as a "vested interest" and may

and United States v. Scott, 167 F. 2d 301 (8 Cir. 1948).

As to the general law as declared by the Federal courts the decision of the Supreme Court in Central Bank of Washington v. Hume, 128 U.S. 195 (1888), is illustrative of features of it. The decision holds, *inter alia*, that it is the general rule that a policy and the money to become due under it, belong, the moment the policy is issued to the person named in it as the beneficiary. The policies of insurance in the Hume case quite possibly did not provide that the insured could change the beneficiary but this feature, as we have indicated, is irrelevant here. Hume was admittedly insolvent at the time the insurance was effected and it was argued that the policies were within the provisions of 13 Elizabeth, c. 5. The Supreme Court was of the view that the statute of 13 Elizabeth governed and held *inter alia* that Hume's creditors were not entitled to recover the premiums paid by him on life insurance policies issued for the benefit of his wife and children. The statute of 13 Elizabeth was designed to prevent conveyances which defeated or delayed creditors. It declares, in substance, that every conveyance made to the end, purpose, and intent to delay, hinder, or defraud creditors and others of their just and lawful actions shall be void, with the proviso that nothing therein contained shall extend to defeat any estate or interest made on good consideration and bona fide to any person having, at the

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not be reached by a creditor, even by the United States. Cf. Sullivan v. Maroney, 76 N.J.Eq. 104, 109, 73 A. 843, 844 (1909), affirmed 77 N.J.Eq. 565, 78 A. 150 (1910), and Phoenix Mut. Life Ins. Co. v. Connelly, 188 F. 2d 462, 464-5 (3 Cir. 1951).

As we have stated the parties have agreed that Herman Bess was solvent when the policies were issued and that he was solvent at all times when premiums were paid. There therefore was no payment of premiums in fraud of creditors and Mrs. Bess was designated as beneficiary at all times save for two small irrelevant periods in respect to only two of the policies. See note 1, *supra*. As to the cash surrender value of the policies, amounting to $3,362.53, though we have found no case in point and none has been cited to us, we are of the opinion that the term "proceeds" as employed in the New Jersey statute means the full amount payable to the beneficiary upon the policy on the death of the insured. It follows therefore that under the law of New Jersey Mrs. Bess may retain the full proceeds of the policies in the instant case without liability for the claim asserted by the United States against her husband for unpaid taxes.

time, no notice of such fraud, 24 Am. Jur., Fraudulent Conveyances § 4, p. 163. See Annotation, 31 A.L.R. 51. The statute of 13 Elizabeth is generally acknowledged to be the principal source of judicial decision as to when a conveyance is fraudulent. *Id.* at p. 164. The statute is declaratory of the existing principles of the common law. *Ibid.* We believe that the governing principles of the general law are as set out in this paragraph.

Coming now to our decision in the Pearlman case we find that the court below interpreted our ruling as requiring it to decide that the proceeds of the policies in the case at bar were transferred to Mrs. Bess[4] on her husband's death. We think that such a conclusion was not warranted by our Pearlman decision[5] nor is it supported by more recent cases.[6] The proceeds of the policies—putting cash surrender values to one side for the time being—were not the property of Herman Bess as required by Section 311(a)(1). He never possessed the right to receive the proceeds and therefore he could not transfer them. Moreover, as we have stated, Bess was solvent when the policies wre issued and solvent at all times when premiums were paid. In the Pearlman case, while Pearlman was solvent when the policies were issued and when some of the premiums were paid, after he became insolvent and up to the time of his death he continued to pay the premiums on the policies. In Pearlman we went no further than the Tax Court which held that the beneficiaries of the policies were transferees as to the cash surrender value of the policies. In the case at bar Mrs. Bess cannot be found to be a transferee of the *proceeds* of the policies under the general law as we have set it out.

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[4] We conclude this because while the proceeds of the policies amounted to $63,576.95, and the judgment in favor of the United States to $11,657.30, the amount of the judgment far exceeded the cash surrender value of the policies which, as we have stated in this opinion, was $3,362.53.

[5] The facts of the case as found by the Tax Court in 4 T.C. 34 (1944) disclose that the cash surrender values of the pertinent policies totaled $51,541 and that the tax liability was $25,713.57. See Rowen v. Commissioner, 215 F. 2d 641, 645 (2 Cir. 1954) on this point.

[6] See United States v. New, 217 F. 2d 166, 167 (7 Cir. 1954), and Rowen v. Commissioner, 215 F. 2d 641, 644 (2 Cir. 1954).

The cash surrender values of the policies in the instant case present a different issue. Bess was adjudicated
32 insolvent more than two years after his death but the account filed by Mrs. Bess as executrix makes it clear that he also was insolvent at the time of death. At the time of his death, as we have stated, the policies possessed a cash surrender or loan value of $3,362.53. He therefore possessed just prior to his death, a chose in action in the amount stated which he could have collected from the insurance companies in accordance with the terms of the policies. The Supreme Court in the Hume case, *supra*, seemed to recognize the payment of premiums as transfers and the incidence of the payments of premiums therefore timed the transfers here. By the terms of the policies in the Hume case nothing passed at the time of Hume's death. So was it here. It is therefore not realistic here, as the court pointed out in Rowen v. Commissioner, *supra*, 215 F. 2d at p. 647, in a like situation, to view Bess's death as wiping out the loan or surrender values. Bess's death was merely a condition on the occurrence of which the loan or surrender values of the policies no longer were payable to him but became merged in the larger values which the insurance companies were obligated to pay to Mrs. Bess. The loan or surrender values were then an item of property and Mrs. Bess was a transferee of them within the meaning of Section 311(a)(1). It follows that the United States is entitled to recover the amount of the loan or surrender values from her.

Other points raised by the parties do not require discussion.

The judgment of the court below will be vacated with the direction to enter judgment for the United States in conformity with this opinion.

* * * * * * * * * *

35 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

UNITED STATES OF AMERICA

vs.

MOLLY G. BESS, *Appellant*

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Present: BIGGS, *Chief Judge,* KALODNER, *Circuit Judge,* and KRAFT, *District Judge.*

Judgment—March 28, 1957

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby vacated, with direction to enter judgment for the United States of America in conformity with the opinion of this Court.

March 28, 1957

37 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

Motion and Order Extending Time to File Petition For Rehearing—April 12, 1957

Motion being made by Molly G. Bess, the Defendant-Appellant herein, through her attorney Morris J. Oppenheim, for extension of time within which to file a petition

for rehearing seeking to clarify the issues preliminary to making application to the Supreme Court of the United States for a writ of certiorari.

It is on this 12th day of April, 1957 ordered that the time within which said Defendant-Appellant may file a Petition For Rehearing be and it is hereby extended to and including the 27 day of April 1957.

KALODNER,
Circuit Judge

* * * * * * * * * *

41 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Docket No. 12,026

UNITED STATES OF AMERICA, *Plaintiff-Appellee,*

v.

MOLLY G. BESS, *Defendant-Appellant*

Petition For Rehearing—Filed April 29, 1957

The defendant-appellant, Molly G. Bess, presents this, her Petition for Rehearing of the above-entitled cause, and, in support thereof, respectfully shows:

1. The appeal herein was argued before this Court on December 4, 1956.

2. On March 28, 1957, this Court rendered its decision vacating the judgment of the District Court and directing entry of judgment in favor of the plaintiff-appellee in accordance with the opinion.

3. The defendant-appellant seeks a rehearing of this cause upon the following grounds:

A.

This case is not "bottomed" on Section 311 of the Internal Revenue Code of 1939 as this Court has assumed in

its opinion and therefore it does not follow that the United States is entitled to recover the loan or surrender value from Mrs. Bess as a transferee within the meaning of Section 311 a (1) as this Court has determined.

This case was tried in the District Court on a stipulation of facts, paragraph 31 of which provides:

> "At no time prior to the institution of this action did the Commissioner of Internal Revenue propose a transferee assessment against defendant under the provisions of Section 311 of the Internal Revenue Code of 1939."

The brief filed on behalf of the plaintiff-appellee, United States of America, states:

> "* * * The Government here is not proceeding under Section 311 of the Internal Revenue Code of 1939 * * *." (Appellee Br. page 27).

B.

This case does not present a "federal tax question" to be "decided on general law as laid down by the Federal Courts" as this Court has assumed in its opinion (Opinion page 3).

No federal tax question is presented.

The assessment for taxes against Herman Bess was tantamount to a judgment. Although as between Herman Bess and the United States the basis for the judgment was a tax, nevertheless as between the defendant-appellant, Molly G. Bess, and the United States, the latter is merely a judgment creditor of Herman Bess, having no greater or different rights than any judgment creditor of Herman Bess regardless of the nature of Bess' debt.

In *Stern* vs. *Commissioner*, also involving transferee liability, decided by the Court of Appeals, 6th Cir., after the case at bar was argued that Court wrote:

> "In this case, *the Government is in no better position than any other creditor*". *Stern* vs. *Commissioner*, 6th Cir., decided 2/26/57, 1957 C. C. H., Par. 9429. (Italics supplied).

43 C.

This case is not governed by the rationale of the *Pearlman* case 153 F. 2d 560 as this Court in its opinion has assumed, since the case at bar is clearly distinguishable in three material respects, namely:

1. In *Pearlman* the Commissioner of Internal Revenue assessed the transferee liability under section 311 Internal Revenue Code of 1939.

In the case at bar on the other hand, no steps were taken to impose liability upon the defendant-appellant under section 311.

2. In *Pearlman* the insured was hopelessly insolvent when he took out the policies, when he changed the beneficiary from his estate to his family and when he paid the premiums. In other words, he definitely diverted to his family money to which his creditors were entitled.

In the case at bar, to the contrary, it is stipulated that Bess was solvent at all times when he paid the premiums, (Stip. 30). In fact, since he had an interest in assets worth $55,241.63 at his death, of substantially greater value than his total liabilities (Stip. 17), the inference of the Court that it is "clear that he also was insolvent at the time of death" is at least debatable.

3. In *Pearlman* this Court determined that the beneficiary was liable "whether reliance is placed on general law as declared by federal courts, *or on Pennsylvania law* * * *" (italics supplied).

To the contrary, this Court has pointed out in its opinion that if the law of New Jersey is applied then the defendant-appellant is not liable in any amount.

44 D.

The Court has determined that this case "should be decided on general law as laid down by the Federal Courts and not * * * subject to the limitation in the law of any state."

In footnote 3 to the opinion the Court has correctly set out the applicable New Jersey law. The footnote concludes:

"It follows therefore that under the law of New Jersey Mrs. Bess may retain the full proceeds of the policies in the instant case without liability for the claim asserted by the United States against her husband for unpaid taxes."

In its opinion entered after the case at bar was argued, the Court of Appeals for the 6th Circuit, reversing the Tax Court, held that the liability, if any, of a life insurance beneficiary for unpaid income taxes of the insured was to be determined by state law. *Stern* v. *Commissioner*, C. A.-6, decided 2/26/57, 1957 C. C. H., Par. 9429.

The Federal statute, 28 U. S. C. A., Par. 1652, (formerly 28 U. S. C. A., Par. 725), June 25, 1948, c. 646, 62 Stat. 944 provides:

"The laws of the several states, except where the Constitution or treaties of the United States or Acts on Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply."

The United States Supreme Court in construing that statute ruled:

"Third. Except in matters governed by the Federal Constitution or by Acts of Congress, the law to be applied in any case is the law of the State. And whether the law of the State shall be declared by its Legislature in a statute or by its highest court in a decision is not a matter of federal concern. There is no federal general common law. Congress has no power to declare substantive rules of common law applicable in a state whether they be local in their nature or 'general', be they commercial law or a part of torts. And no clause in the Constitution purports to confer such a power upon the federal courts."

Since the case at bar is not "bottomed" on Section 311 of the Internal Revenue Code of 1939; since it is not a "tax" case; and particularly since Congress has not legislated the substantive law respecting transferee liability (Section 311 is procedural only), and neither "the Consti-

tution or treaties of the United States or Acts of Congress otherwise require or provide" the law of the State of New Jersey governs the law to be applied in this case.

Conclusion

For the reasons set forth above it is respectfully urged that rehearing be granted.

Respectfully submitted,

Morris J. Oppenheim,
Counsel for Defendant-Appellant.

Certificate of Counsel

I Hereby Certify that the foregoing Petition for Rehearing is presented in good faith and not for delay in accordance with Rule 33 of the Rules of this Court.

Morris J. Oppenheim,
Counsel for Defendant-Appellant.

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47 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

(Title omitted)

Order Denying Petition for Rehearing—May 20, 1957

Present: Biggs, *Chief Judge,* and Kalodner, *Circuit Judge,* and Kraft, *District Judge.*

After due consideration the petition for rehearing in the above-entitled case is hereby denied.

By the Court
Biggs,
Chief Judge.

Dated: May 20, 1957

* * * * * * * * * * *

49 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

(Title omitted)

Order Staying Issuance of Mandate—May 29, 1957

Pursuant to Rule 36 (2) of this Court, it is ORDERED that issuance of the mandate in the above cause be, and it is hereby stayed until June 24, 1957.

BIGGS,
Chief Judge.

May 29, 1957

* * * * * * * * * *

51 (File endorsement omitted)

IN UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

No. 12,026

(Title omitted)

Motion and Order Further Staying Issuance of Mandate—June 28, 1957

Motion being made by Molly G. Bess, the Defendant-Appellant herein, through her attorney, Morris J. Oppenheim, for a further stay of mandate on the ground that it is desired to make application to the Supreme Court of the United States for a writ of certiorari, or to take such other steps as may be provided by the rules and by law for review or further consideration,

It is on this 28th day of June, 1957 ordered that the issuance of the mandate in this case be and it hereby is stayed for a period of 30 days from the date hereof.

BIGGS,
Chief Judge.

Consent is given to the entry of this order.

/s/ Morris J. Oppenheim
MORRIS J. OPPENHEIM
/s/ Charles K. Rice,
CHARLES K. RICE
Assistant Attorney General.

* * * * * * * * * *

55 Clerk's Certificate to foregoing transcript omitted in printing.

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57 SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1956

No. ——

UNITED STATES OF AMERICA, *Petitioner*

vs.

MOLLY G. BESS, *Transferee*

Order Extending Time to File Petition for Writ of Certiorari—June 21, 1957

UPON CONSIDERATION of the application of counsel for petitioner,

IT IS ORDERED that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including August 23, 1957.

WILLIAM J. BRENNAN, JR.,
Associate Justice of the Supreme Court of the United States.

Dated this 21st day of June, 1957.

* * * * * * * * * *

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1957

No. ——

MOLLY G. BESS, *Petitioner,*

vs.

UNITED STATES OF AMERICA

Order Extending Time to File Petition for Writ of Certiorari—August 9, 1957

UPON CONSIDERATION of the application of counsel for titioner,

IT IS ORDERED that the time for filing petition for writ of rtiorari in the above-entitled cause be, and the same is reby, extended to and including September 19, 1957.

WILLIAM J. BRENNAN, JR.
Associate Justice of the Supreme Court of the United States.

Dated this 9th day of August, 1957.

* * * * * * * * *

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1957

Nos. 395 and 410

UNITED STATES OF AMERICA, *Petitioner,*

vs.

MOLLY G. BESS; and
MOLLY G. BESS, *Petitioner,*

vs.

UNITED STATES OF AMERICA

Order Allowing Certiorari—October 28, 1957

The petitions herein for writs of certiorari to the United ates Court of Appeals for the Third Circuit are granted.

The cases are consolidated and transferred to the summary calendar with a total of one hour allowed for oral argument. The cases are assigned for argument immediately following No. 311.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petitions shall be treated as though filed in response to such writ.

Supreme Court, U.S.
FILED
AUG 23 1957
JOHN T. FEY, Clerk

LIBRARY
SUPREME COURT, U.S.

No. 395

In the Supreme Court of the United States

OCTOBER TERM, 1957

UNITED STATES OF AMERICA, PETITIONER

v.

MOLLY G. BESS

ETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

J. LEE RANKIN,
Solicitor General,
JOHN N. STULL,
Acting Assistant Attorney General,
A. F. PRESCOTT,
KENNETH E. LEVIN,
Attorneys,
Department of Justice, Washington 25, D. C.

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CITATIONS

Case:

Stern v. *Commissioner*, 242 F. 2d 322, petition for certiorari pending, No. 311, this Term 4, 5

Statutes:

Internal Revenue Code of 1939:

Sec. 311 (26 U. S. C. 1952 ed., Sec. 311) 2, 14

Sec. 3670 (26 U. S. C. 1952 ed., Sec. 3670) 2, 4, 14

In the Supreme Court of the United States

OCTOBER TERM, 1957

No. ——

UNITED STATES OF AMERICA, PETITIONER

v.

MOLLY G. BESS

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

The Solicitor General, on behalf of the United States, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit in this case.

OPINIONS BELOW

The opinion of the District Court (R. 11a–17a)[1] is reported at 134 F. Supp. 467. The opinion of the Courts of Appeals (Appendix A, *infra*, pp. 6–13) is reported at 243 F. 2d 675.

JURISDICTION

The judgment of the Court of Appeals was entered on March 28, 1957. (Appendix A, *infra*, p. 13.) On June 21, 1957, by order of Mr. Justice Brennan, the

[1] Record references are to the appendix of the Court of Appeals brief for Molly G. Bess, appellant in that court.

time for petitioning for a writ of certiorari was extended to August 23, 1957. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1254.

QUESTION PRESENTED

Decedent, Herman Bess, was indebted to the Government for income taxes. He had various life insurance policies as to which he retained, during his life, the right to draw cash surrender values and the right to change the beneficiary. He died leaving an insolvent estate. Respondent, his widow, is the designated beneficiary under the policies. The question is whether respondent is liable as transferee to the full extent of the net proceeds of the policies.

STATUTES INVOLVED

The pertinent provisions of Sections 311 (a) and (f) and 3670 of the Internal Revenue Code of 1939 are set forth in Appendix B, *infra,* pp. 14–15.

STATEMENT

Herman Bess, husband of respondent Molly G. Bess, died insolvent on June 29, 1950. (R. 3a, 5a.)

Prior to Bess's death, the Commissioner had assessed against him (on July 30, 1948) a deficiency for the year 1945 in the total sum of $11,541, consisting of $10,119.31 additional income tax plus $1,421.69 interest thereon. On the same date, the Commissioner assessed a deficiency for the year 1946 of $3,789.32, consisting of $3,507.03 additional tax and $282.29 interest. On August 24, 1950, the Commissioner assessed against Bess's estate for the year 1947 a deficiency of $925.94, composed of $813.22 additional income tax

and $112.72 interest thereon. In each case, notice and demand were made on decedent or his estate. Bess made partial payment of these deficiencies prior to his death, and his executrix made some payments after his death, leaving a total of $8,874.57 still unpaid. (R. 3a–4a.)

At the time of his death, Herman Bess carried eight insurance policies on his life with a total cash surrender value of $3,362.53 (R. 7a–10a), and total proceeds of $63,576.95. Molly G. Bess was the beneficiary of these policies. (R. 7a.) On all of the policies, Herman Bess had paid the premiums (R. 10a) and had retained the right to change the beneficiary (R. 7a–10a). With the exception of No. 8, a group insurance policy in the face amount of $2,500, decedent had retained the right to borrow against the cash surrender values and to assign the policies. (R. 7a–10a.)

By reason of the death of Herman Bess, Molly G. Bess, as beneficiary of the policies, became entitled to be paid according to their terms and has in fact received a total sum of $69,576.95. (R. 10a.)

The District Court held that Molly G. Bess was liable for the delinquent taxes of Herman Bess as the transferee of the proceeds of his policies. (R. 11a–17a.) The Court of Appeals vacated the judgment of the District Court, holding that Molly G. Bess was the transferee of the cash surrender values of the policies, which were property of Herman Bess prior to his death, but that she was not the transferee of the full proceeds of the policies, which were not the property of Herman Bess during his lifetime. The Court of Appeals held further that Molly G. Bess's

liability as the transferee of the cash surrender values was imposed by federal law and was not subject to state law limitations.[2] (Appendix A, *infra*, pp. 6–13.)

REASONS FOR GRANTING THE WRIT

Stern v. *Commissioner*, 242 F. 2d 322 (C. A. 6), petition for certiorari pending, No. 311, this Term, similarly involves a beneficiary of the life insurance policies of a delinquent taxpayer. As here, the insured retained, during his lifetime, the right to change the beneficiary and to draw the cash surrender values; as here, he died leaving an insolvent estate. The Sixth Circuit held that the beneficiary was not a transferee either of the surrender values of the policies or the proceeds thereof. It ruled further that the liability of a transferee for taxes owed by the transferor is subject to limitations imposed by state law. On July 25, 1957, the Government petitioned for a writ of certiorari in the *Stern* case, requesting this Court to consider (1) the beneficiary's liability as a transferee of the cash surrender values and (2) the beneficiary's liability for the full proceeds. We pointed out in our petition that there was a conflict as to the first question (with the instant *Bess* case) and that the second question was a closely related and an important one.

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[2] The Government had argued also that, by reason of assessments against decedent prior to his death, a lien had attached to all of his property, and that this was a proceeding to enforce the lien. See Section 3670 of the 1939 Code, *infra*, pp. 14–15. The Court of Appeals ignored this contention in its opinion. If certiorari is granted, the Government reserves the right to assert this alternative basis of recovery.

In the instant case, the Third Circuit has sustained the Commissioner's position that cash surrender values are reachable in the hands of the beneficiary (*infra*, pp. 12–13). It has also ruled that the question of transferee liability is exclusively a federal one and that state law limitations are accordingly inapplicable (*infra*, pp. 7–11). However, the court below agreed with the Sixth Circuit that net proceeds, as distinguished from cash surrender values, are not reachable.

If this Court should undertake to review in the *Stern* case the second question there presented, *i. e.*, the question of liability for the full proceeds of the policies, we believe that it should also grant review in the instant case.[3] For a fuller statement of the reasons why we believe this issue is one meriting the consideration of this Court, we respectfully refer to our petition in No. 311.

CONCLUSION

This petition for a writ of certiorari should be granted.

Respectfully submitted.

J. LEE RANKIN,
Solicitor General.
JOHN N. STULL,
Acting Assistant Attorney General.
A. F. PRESCOTT,
KENNETH E. LEVIN,
Attorneys.

AUGUST 1957.

[3] We are informed that respondent, Mrs. Bess, is filing a cross-petition challenging the Third Circuit's ruling that there was liability to the extent of the cash surrender values.

APPENDIX A

1. Opinion of the Court of Appeals

No. 12026

In the United States Court of Appeals For the Third Circuit

UNITED STATES OF AMERICA

v.

MOLLY G. BESS, APPELLANT

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Argued December 4, 1956

Before BIGGS, *Chief Judge*, KALODNER, *Circuit Judge*, and KRAFT, *District Judge*.

OPINION OF THE COURT

(Filed March 28, 1957)

By BIGGS, *Chief Judge*.

The court below gave judgment in favor of the United States against the defendant, Molly G. Bess, widow of Herman Bess, on the theory that under Section 311 of the 1939 Code, 26 USCA (I. R. C. 1939) § 311, the defendant was a transferee of property of a taxpayer, her husband, who owed the government delinquent income taxes.

The facts are not in dispute. The defendant's husband died on June 29, 1950. At the time of his death there were in force eight insurance policies on his life. Seven of the policies were issued during

1934, 1935, 1936, and 1937. The eighth, a group insurance policy with no cash value, was issued June 19, 1950. Herman Bess had the right to change the beneficiary of the policies and also had the right to borrow upon the security of the cash surrender value of the seven policies described first herein. The defendant was named as beneficiary when the policies were issued to Herman Bess, and, except for temporary changes with respect to two policies,[1] the defendant remained the beneficiary. The government and the defendant have assumed, without dispute, that Herman Bess was solvent when the policies were issued, and have stipulated that he was solvent when the premiums were paid. The total cash surrender or loan value of all the policies was $3,362.53 at the time of Bess's death. The defendant received $63,576.95 as the total proceeds of the eight policies.

On July 17, 1952, more than two years after his death, the estate of Herman Bess was adjudged insolvent. Part payment has been made on the claims of the United States for income taxes owed by Herman Bess, but a balance of $8,874.57 remains unpaid. The United States instituted suit against the defendant for that amount plus interest from the date of assessment and was awarded judgment in the sum of $11,657.30. 134 F. Supp. 467 (D. N. J. 1955). Mrs. Bess has appealed.

The statute on which the alleged liability of the defendant is bottomed is Section 311 of the 1939 Internal Revenue Code, 26 USCA (I. R. C. 1939) § 311,

[1] In one policy the beneficiary was changed from the defendant to the insured's estate on April 4, 1945, and on the same day the defendant was redesignated as the beneficiary; in another policy the beneficiary was changed from the defendant to the insured's estate on March 23, 1945, and on April 3, 1945 the defendant was redesignated as the beneficiary.

set out in the margin.[2] It is the universal view that the statute created no new substantive rights and liabilities and that the only liabilities to be enforced thereunder are those existing in law or in equity when the enforcement proceeding is begun. *Pearlman v. Commissioner,* 153 F. 2d 560, 561–2 (3 Cir. 1946), and *Rowen v. Commissioner,* 215 F. 2d 641, 643 (2 Cir. 1954). Herman Bess was domiciled in New Jersey up to his death. His widow's domicil remains there. In *Pearlman v. Commissioner, supra,* at p. 562, we stated that "On principle the question [as to the existence or non-existence of liability on the part of the widow] seems to us clearly to be one to be answered without reference to state law limitations." We also said, since we had before us a husband domiciled in Pennsylvania until his death with his wife's domicil remaining there, that "Whether the reliance is placed on general law as declared by federal courts, or on Pennsylvania law, we think the conclusion of the Tax Court must stand." We may

[2] Section 311 provides in pertinent part: "Transferred assets—(a) Method of collection. The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) Transferees. The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter.

* * * * * *

"(f) Definition of 'transferee'. As used in this section, the term 'transferee' includes heir, legatee, devisee, and distributee."

perhaps remark here, without cynicism, that a declaration on principle is not necessarily a declaration of law, but we went on to say that we preferred to rest the decision on the wider ground that since there was a federal tax question to be decided it should be decided on general law as laid down by the Federal courts and not be subject to the limitation in the law of any State. We adhere to our former ruling but since this case may reach the reviewing Court, other Courts of Appeals having reached the contrary conclusion, *Rowen* v. *Commissioner, supra,* and the authorities cited therein, 215 F. 2d at 648–9, we have set out what we believe to be the status of Mrs. Bess under the law of New Jersey, were that law applicable, in *footnote 3 below.* Cf. *Poe* v. *Seaborn,* 282

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[3] As to the law of New Jersey the applicable sections are New Jersey R. S. 17:34–28 and 17:34–29; NJSA 17:34–28 and NJSA 17:34–29. Section 29 provides that every policy of life insurance made payable to or issued for the benefit of a married woman, or after its issue assigned or in any way made payable to a married woman, whether by her husband or by any other person, shall "inure to her separate use and benefit * * *" according to its terms unless premiums were paid in fraud of creditors as set out in Section 28. There can be no doubt that in the absence of fraud on creditors in the payment of premiums or assignment of the beneficial interest to some person other than to the wife, the wife's interest in the proceeds of a policy has a status described by the law of New Jersey as a "vested interest" and may not be reached by a creditor, even by the United States. Cf. *Sullivan* v. *Maroney,* 76 N. J. Eq. 104, 109, 73 A. 843, 844 (1909), affirmed 77 N. J. Eq. 565, 78 A. 150 (1910), and *Phoenix Mut. Life Ins. Co.* v. *Connelly,* 188 F. 2d 462, 464–5 (3 Cir. 1951).

As we have stated the parties have agreed that Herman Bess was solvent when the policies were issued and that he was solvent at all times when premiums were paid. There therefore was no payment of premiums in fraud of creditors and Mrs. Bess was designated as beneficiary at all times save for two small irrelevant periods in respect to only two of the

U. S. 101 (1930); and *United States* v. *Scott*, 167 F. 2d 301 (8 Cir. 1948).

As to the general law as declared by the Federal courts the decision of the Supreme Court in *Central Bank of Washington* v. *Hume*, 128 U. S. 195 (1888), is illustrative of features of it. The decision holds, *inter alia*, that it is the general rule that a policy and the money to become due under it, belong, the moment the policy is issued to the person named in it as the beneficiary. The policies of insurance in the *Hume* case quite possibly did not provide that the insured could change the beneficiary but this feature, as we have indicated, is irrelevant here. Hume was admittedly insolvent at the time that the insurance was effected and it was argued that the policies were within the provisions of 13 Elizabeth, c. 5. The Supreme Court was of the view that the statute of 13 Elizabeth governed and held *inter alia* that Hume's creditors were not entitled to recover the premiums paid by him on life insurance policies issued for the benefit of his wife and children. The statute of 13 Elizabeth was designed to prevent conveyances which defeated or delayed creditors. It declares, in substance, that every conveyance made to the end, purpose, and intent to delay, hinder, or defraud creditors and others of their just and lawful actions shall be void, with the proviso that nothing therein con-

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policies. See note 1, *supra*. As to the cash surrender value of the policies, amounting to $3,362.53, though we have found no case in point and none has been cited to us, we are of t opinion that the term "proceeds" as employed in the New Jersey statute means the full amount payable to the beneficiary upon the policy on the death of the insured. It follows therefore that under the law of New Jersey Mrs. Bess may retain the full proceeds of the policies in the instant case without liability for the claim asserted by the United States agafnst her husband for unpaid taxes.

tained shall extend to defeat any estate or interest made on good consideration and bona fide to any person having, at the time, no notice of such fraud. 24 Am. Jur., Fraudulent Conveyanace § 4, p. 163. See Annotation, 31 A. L. R. 51. The statute of 13 Elizabeth is generally acknowledged to be the principal source of judicial decision as to when a conveyance is fraudulent. *Id.* at p. 164. The statute is declaratory of the existing principles of the common law. *Ibid.* We believe that the governing principles of the general law are as set out in this paragraph.

Coming now to our decision in the *Pearlman* case we find that the court below interpreted our ruling as requiring it to decide that the proceeds of the policies in the case at bar were transferred to Mrs. Bess[4] on her husband's death. We think that such a conclusion was not warranted by our Pearlman decision[5] nor is it supported by more recent cases.[6] The proceeds of the policies—putting cash surrender values to one side for the time being—were not the property of Herman Bess as required by Section 311 (a) (1). He never possessed the right to receive the proceeds and therefore he could not transfer them. Moreover, as we have stated, Bess was solvent when the policies were issued and solvent at all times when premiums were

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[4] We conclude this because, while the proceeds of the policies amounted to $63,576.95, and the judgment in favor of the United States to $11,657.30, the amount of the judgment far exceeded the cash surrender value of the policies which, as we have stated in this opinion, was $3,362.53.

[5] The facts of the case as found by the Tax Court in 4 T. C. 34 (1944) disclose that the cash surrender values of the pertinent policies totaled $51,541 and that the tax liability was $25,713.57. See *Rowen* v. *Commissioner*, 215 F. 2d 641, 645. (2 Cir. 1954) on this point.

[6] See *United States* v. *New*, 217 F. 2d 166, 167 (7 Cir. 1954), and *Rowen* v. *Commissioner*, 215 F. 2d 641, 644 (2 Cir. 1954).

paid. In the *Pearlman* case, while Pearlman was solvent when the policies were issued and when some of the premiums were paid, after he became insolvent and up to the time of his death he continued to pay the premiums on the policies. In *Pearlman* we went no further than the Tax Court which held that the beneficiaries of the policies were transferees as to the cash surrender value of the policies. In the case at bar Mrs. Bess cannot be found to be a transferee of the *proceeds* of the policies under the general law as we have set it out.

The cash surrender values of the policies in the instant case present a different issue. Bess was adjudicated insolvent more than two years after his death but the account filed by Mrs. Bess as executrix makes it clear that he also was insolvent at the time of death. At the time of his death, as we have stated, the policies possessed a cash surrender or loan value of $3,362.53. He therefore possessed just prior to his death, a chose in action in the amount stated which he could have collected from the insurance companies in accordance with the terms of the policies. The Supreme Court in the *Hume* case, *supra,* seemed to recognize the payment of premiums as transfers and the incidence of the payments of premiums therefore timed the transfers here. By the terms of the policies in the *Hume* case nothing passed at the time of Hume's death. So was it here. It is therefore not realistic here, as the court pointed out in *Rowen* v. *Commissioner, supra,* 215 F. 2d at p. 647, in a like situation, to view Bess's death as wiping out the loan or surrender values. Bess's death was merely a condition on the occurrence of which the loan or surrender values of the policies no longer were payable to him but became merged in the larger values which the insurance companies were obligated to pay to Mrs.

Bess. The loan or surrender values were then an item of property and Mrs. Bess was a transferee of them within the meaning of Section 311 (a) (1). It follows that the United States is entitled to recover the amount of the loan or surrender values from her.

Other points raised by the parties do not require discussion.

The judgment of the court below will be vacated with the direction to enter judgment for the United States in conformity with this opinion.

2. Judgment of the Court of Appeals

[Caption omitted]

[Filed March 28, 1957]

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby vacated, with direction to enter judgment for the United States of America in conformity with the opinion of this Court.

APPENDIX B

Internal Revenue Code of 1939:

SEC. 311. TRANSFERRED ASSETS.

(a) *Method of Collection.*—The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

(1) *Transferees.*—The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter.

* * * * *

Any such liability may be either as to the amount of tax shown on the return or as to any deficiency in tax.

* * * * *

(f) *Definition of "Transferee".*—As used in this section, the term "transferee" includes heir, legatee, devisee, and distributee.

(26 U. S. C. 1952 ed., Sec. 311.)

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, addi-

tional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U. S. C. 1952 ed., Sec. 3670.)

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SUPREME COURT, U. S.

Nos. 395 and 410

In the Supreme Court of the United States

OCTOBER TERM, 1957

UNITED STATES OF AMERICA, PETITIONER

v.

MOLLY G. BESS

MOLLY G. BESS, PETITIONER

v.

UNITED STATES OF AMERICA

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

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In the Supreme Court of the United States

OCTOBER TERM, 1957.

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UNITED STATES OF AMERICA

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES

OPINIONS BELOW

The opinion of the District Court (R. 10–16) is reported at 134 F. Supp. 467. The opinion of the Court of Appeals (R. 17–22) is reported at 243 F. 2d 675.

JURISDICTION

The judgment of the Court of Appeals was entered on March 28, 1957 (R. 23). On May 20, 1957, the

petition of Molly G. Bess for rehearing was denied (R. 28). On June 21, 1957, by order of Mr. Justice Brennan, the time for filing a petition for certiorari on behalf of the United States was extended to and including August 23, 1957 (R. 30). The petition of the United States was filed on August 22, 1957. The petition of Molly G. Bess was filed on August 29, 1957. The writs were granted on October 28, 1957 (R. 31–32). The jurisdiction of this Court rests upon 28 U. S. C. 1254.

QUESTION PRESENTED

Whether, for the purpose of collecting federal income taxes and particularly those as to which a lien attached on decedent's property before his death, the beneficiary of life insurance policies, in which the decedent had retained the right to change the beneficiary and to draw, or borrow against, the cash surrender values, is liable to the Government to the extent (1) of the entire proceeds of the policies, or, alternatively, (2) of the cash surrender values.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are: Sections 311 (a) and (f), 811 (g), 827 (b), 900 (a) and (e) and 3670 of the Internal Revenue Code of 1939; Section 316 of the Revenue Act of 1926; Sections 34–28 and 34–29 of 17 New Jersey Statutes Annotated; Section 81.27 of Treasury Regulations 105; and Section 29.311–1 of Treasury Regulations 111.

Section 3670 of the Internal Revenue Code of 1939 provides:

Property Subject to Lien

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person.

(26 U. S. C. 3670.)

17 New Jersey Statutes Annotated (Permanent ed.) provides:

17:34–28. *Beneficiary's right to proceeds*

When a policy of insurance is effected by any person on his own life, or on another life in favor of a person other than himself having an insurable interest therein, the lawful beneficiary thereof, other than himself or his legal representatives, shall be entitled to its proceeds, against the creditors and representatives of the person effecting it. The person to whom a policy of life insurance is made payable may maintain an action thereon in his own name. Subject to the statute of limitations, the amount of any premiums for the insurance paid in fraud of creditors, with interest thereon, shall, however, inure to their benefit from the proceeds of the policy, but the company issuing the policy shall be discharged of all liability thereon by payment of its proceeds in accordance with its terms, unless, before the payment, the company shall have written notice by or in behalf of some creditor, with specification of the amount claimed, claiming to recover

for certain premiums paid in fraud of creditors.

17:34–29. *Policies to inure to benefit of married woman*

Every policy of life insurance made payable to or for the benefit of a married woman, or after its issue assigned, transferred or in any way made payable to a married woman, or to any person in trust for her or for her benefit, whether procured by herself, her husband or by another person, and whether the assignment or transfer is made by her husband or by another person, shall inure to her separate use and benefit, and to that of her children, according to the terms and provisions of the policy or assignment, subject to the foregoing provisions relating to premiums paid in fraud of creditors.

The remainder of the statutes and regulations referred to above are set out in the appendix to the Government's brief in *Commissioner of Internal Revenue* v. *Stern*, No 311, this Term.

STATEMENT

Herman Bess, husband of Molly G. Bess, died on June 29, 1950 (R. 3), leaving an insolvent estate (R. 5, 22).

Prior to Mr. Bess's death, the Commissioner had assessed against him on July 30, 1948, a deficiency for the year 1945 in the total amount of $11,514, consisting of $10,119.31 additional income tax plus $1,421.69 interest thereon. On the same date, the Commissioner assessed a deficiency for the year 1946 of $3,789.32, consisting of $3,507.03 additional tax

and $282.29 interest. In each case, notice and demand were made on decedent. (R. 4.) On August 24, 1950, the Commissioner assessed a deficiency for the year 1947 of $925.94, consisting of $813.22 additional tax and $112.72 interest thereon. Notice and demand were made on decedent's estate. (R. 5). Herman Bess made partial payment of the deficiency for 1945 prior to his death, and his executrix made some additional payments thereafter, leaving $4,159.31 plus interest due and unpaid for that year. No part of the amounts due for 1946 and 1947 has been paid. (R. 4–5.)

At the time of his death, Herman Bess carried eight insurance policies on his life with a total cash surrender value, as reduced by outstanding loans, of $3,362.53, and total proceeds of $63,576.95 (R. 7–10). Molly G. Bess was the beneficiary of those policies (R. 7). On all of them, Mr. Bess had paid the premiums (R. 9) and had retained the right to change the beneficiary (R. 7–9). Except for policy No. 8, a group insurance policy, Bess had retained the right to draw the cash surrender values or borrow against them and to assign the policies (R. 7–9).

By reason of the death of Herman Bess, Molly G. Bess as beneficiary of the policies became entitled to be paid according to their terms and has in fact received a total sum of $69,576.95 (R. 9).[1]

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[1] This is the stipulated figure with no indication in the record as to why the beneficiary received $6,000 more than the $63,576.95 provided in the policies. The correctness of the figure is not important to the case.

The District Court held that Molly G. Bess was liable as a transferee of the proceeds of decedent's insurance policies for the entire amount of decedent's delinquent income taxes (R. 10–16). The Court of Appeals vacated the judgment of the District Court, and held that Molly G. Bess was liable as a transferee only to the extent of the cash surrender values of the policies (R. 17–23).

SUMMARY OF ARGUMENT

This proceeding was brought in equity by the United States to enforce transferee liability against Molly G. Bess as beneficiary of the life insurance policies of her deceased husband, Herman Bess, who died owing delinquent income taxes and whose estate is insolvent. Except that for two of the three years here involved the Government has a tax lien on all the property and rights to property of the insured prior to his death, the facts in the instant case do not differ materially from those in the companion case of *Commissioner of Internal Revenue* v. *Stern*, No. 311, this Term. In the present case, the Government proceeded against the beneficiary in equity rather than by the summary method authorized by Section 311 of the Internal Revenue Code of 1939 which was followed in the *Stern* case. Since Section 311 added nothing of substance to transferee liability, the question whether the beneficiary here is liable as a transferee, and to what extent, must be decided upon the same principles asserted by the Government in its brief in *Stern*. Rather than restating that argument in detail here, we respectfully refer the Court to our brief in that case.

Although New Jersey law holds, unlike Kentucky, that the interest of the beneficiary of insurance policies is "vested," the New Jersey cases show plainly that, where the insured reserves the rights retained by the insured here, the so-called "vested" interest of the beneficiary is subject to defeasance and is no greater than the mere "expectancy" involved in the *Stern* case. Thus, the beneficiary here had no more actual rights in the policies prior to the death of the insured than did the beneficiary in *Stern*. Furthermore, since the New Jersey statute relied on by the beneficiary here is, like the Kentucky statute in *Stern*, an exemption statute, it is clearly not available to limit the beneficiary's liability, for the reasons stated in our brief in *Stern*.

This case presents one additional ground, not involved in the *Stern* case, for refusing to recognize the exemption provided by state law. Here, the Commissioner in two of the years involved assessed the deficiencies and gave notice and demand for payment to the original taxpayer before his death. Under Section 3670 of the Internal Revenue Code of 1939, *supra* p. 3, a lien thereupon attached to "all property and rights to property" of the taxpayer. Therefore, if, as we urge, the beneficiary of the policies was the transferee of the proceeds or of the cash surrender values of those policies, they came to her subject to an existing lien. It is well established that state law will not be permitted to destroy a federal lien. Even those courts which have not looked with favor upon following the proceeds or cash surrender values of insurance generally have permitted it when a lien has

attached during the insured's life. *United States* v. *Behrens*, 230 F. 2d 504 (C. A. 2), certiorari denied, 351 U. S. 919; *United States* v. *Hoper*, 242 F. 2d 468 (C. A. 7).

ARGUMENT

I

Regardless of state exemptions, the beneficiary of life insurance policies as to which the insured retained certain rights is liable as a transferee either as to the entire proceeds or, alternatively, as to the cash surrender values

In the companion case of *Commissioner of Internal Revenue* v. *Stern*, No. 311, this Term, the Government urged that the beneficiary of life insurance policies, as to which the insured had reserved the rights to change the beneficiary and to draw, or to borrow against, the cash surrender values, is liable for the insured's delinquent income taxes as a transferee, either as to the entire proceeds or, alternatively, as to the cash surrender values. The facts in this case do not differ materially from *Stern* except that here the Government had a tax lien for two of the three tax years involved on all the property and rights to property of the insured prior to his death. In the next portion of this brief, we urge that this factor presents an additional basis for our argument that the state exemption law is inapplicable.

The procedure followed by the Government in the two cases also differs. In *Stern*, the Government proceeded against the beneficiary under the provisions of Section 311 of the Internal Revenue Code of 1939. It asserted a deficiency against the beneficiary who thereupon petitioned the Tax Court for a

redetermination. In the present case, the Government did not proceed against the beneficiary by the summary method authorized in Section 311, but rather brought an action against her in equity, as it had the right to do. *Leighton* v. *United States*, 289 U. S. 506. As set forth in more detail in the *Stern* brief, Section 311 added nothing of substance to transferee liability, so the question here of whether the beneficiary is liable as a transferee, and to what extent, must be decided upon the same principles asserted by the Government in its brief in *Stern*.

Essentially, our position in both cases is that, because the insured decedents retained the right until their deaths to change the beneficiaries of their life insurance policies and could, therefore, have made their estates the beneficiaries, the designation of the wives as beneficiaries, coupled with the non-exercise of the right to change the designation to their estates, made the wives transferees of the entire proceeds of the policies, and liable as such for the decedents' delinquent taxes. Alternatively, we argue that, since the insureds retained the right to draw, or to borrow against, the cash surrender value of their policies (with the exception of one policy in this case), those values were assets belonging to them. In this respect the court below upheld the Government's position, ruling that the cash surrender value of a policy is not wiped out by the death of the insured but merges into the proceeds and is subject to transferee liability on the basis of general federal law. Rather than restate the arguments in full, we respectfully refer the Court to our brief in the *Stern* case.

Unlike Kentucky (*Metropolitan Life Ins. Co.* v. *Tye*, 288 Ky. 750; *Hoskins* v. *Hoskins*, 231 Ky. 5), New Jersey holds that the interest of the beneficiary of a life insurance policy is "vested." *Metropolitan Life Ins. Co.* v. *Woolf*, 138 N. J. Eq. 450; *Prudential Ins. Co. of America* v. *Swanson*, 111 N. J. Eq. 477. The decisions show, however, that where the insured reserves the rights retained by the insured here, the so-called "vested" right of the beneficiary is subject to defeasance, an interest actually no greater than the mere "expectancy" involved in the *Stern* case. *Phœnix Mut. Life Ins. Co.* v. *Connelly*, 188 F. 2d 462 (C. A. 3). In that case the insured had retained the right to change the beneficiary and to assign the policy. Without changing the beneficiary, the insured assigned the policy as collateral for a loan, and the question was whether or not the assignee could recover the amount of the loan out of the proceeds of the policy even though the beneficiary's interest under state law was "vested." The court held that he could, saying (pp. 464, 465, 466):

> However, it is equally important and as clearly recognized by the courts of New Jersey that primary definition and delimitation of the interest of the beneficiary must be found in and measured by the terms of the contract of insurance out of which solely his rights arise. * * *
>
> * * * * * *

> The reservation in the policy of additional rights to the insured simply subjects the interest of the beneficiary in and from its inception to additional powers of defeasance. * * *
>
> * * * * *
>
> The act of assignment was the exercise of a power reserved to the insured by the terms of the contract to affect both his rights and those of the beneficiary. Both were subordinated to the rights of the assignee.

Thus, the beneficiary here had no more actual rights in the decedent's insurance policies before his death than did the beneficiary in the *Stern* case.

Like the Kentucky statute involved in *Stern*, the New Jersey statute, 17 New Jersey Statutes Annotated (Permanent ed.), Sections 34–28 and 34–29, *supra*, pp. 3 and 4, relied on by the beneficiary in the court below, is an exemption statute, and has been labeled as such by the New Jersey courts and the local federal courts. *Slurszberg* v. *Prudential Insurance Co.*, 15 N. J. Misc. 423, 425–426; *In re Pinals*, 38 F. 2d 117, 122 (D. N. J.), affirmed *sub nom. Smith* v. *Metropolitan Life Ins. Co.*, 43 F. 2d 74 (C. A. 3); *Greiman* v. *Metropolitan Life Ins. Co.*, 96 F. 2d 823, 825 (C. A. 3). Clearly, the New Jersey statute is an exemption statute and not available to limit the liability of the transferee here, for the reasons stated in our brief in *Stern*.

II

By reason of the assessment, notice, and demand for payment of decedent's 1945 and 1946 taxes prior to his death, a lien attached to all his property and rights to property, including his insurance, and remains enforceable against that property in the hands of the beneficiary

As pointed out above, a difference of fact exists between this case and *Stern* which, we submit, entitled the Government to recovery of decedent's tax liability for the years 1945 and 1946 on an additional ground. In *Stern*, the insured died prior to any assessments against him by the Commissioner. Here, the Commissioner assessed deficiencies against the insured prior to his death in the amount of $11,514 (consisting of $10,119.31 additional income tax plus $1,421.69 interest) for the year 1945, and the amount of $3,789.32 (consisting of $3,507.03 additional tax and $282.29 interest) for the year 1946. In each case, notice and demand were made on decedent. The deficiency for the year 1947 of $925.94, composed of $813.22 additional income tax and $112.72 interest, was not assessed until after the insured's death and is not involved in the argument made in this point. The insured made partial payment of the deficiency for 1945 prior to his death, and his executrix made some additional payments thereafter, leaving $4,159.31 plus interest due and unpaid for that year. No part of the amount assessed for 1946 has been paid.

Under Section 3670 of the Internal Revenue Code of 1939 (26 U. S. C. 3670, *supra*, p. 3), a lien attached to all the decedent's property and rights to

property by reason of the assessment, notice and demand, and nonpayment occurring prior to his death. The Government urges that this lien applied to the payments made to the beneficiary to the extent not only of the cash surrender value but also of the total proceeds.

Numerous courts have held that such a lien attaches to the cash surrender value of insurance policies, since, in accordance with our argument in *Stern*, these are clearly assets of the decedent during his lifetime. *United States* v. *Metropolitan Life Ins. Co.*, decided January 14, 1958 (C. A. 4); *Knox* v. *Great West Life Assur. Co.*, 109 F. Supp. 207 (E. D. Mich.), affirmed *per curiam*, 212 F. 2d 784 (C. A. 6); *Smith* v. *Donnelly*, 65 F. Supp. 415 (E. D. La.); *United States* v. *Ison*, 67 F. Supp. 40 (S. D. N. Y.); *United States* v. *Prudential Ins. Co. of America*, 54 F. Supp. 664 (E. D. Pa.); *United States* v. *Royce Shoe Co.*, 137 F. Supp. 786 (D. N. H.); *United States* v. *Trout*, 46 F. Supp. 484 (S. D. Cal.). We submit further, in accord with our argument in Point II of the *Stern* brief and the holding of the court below, that these surrender values are not wiped out upon the death of the insured, but rather merge in the proceeds. As a result, the lien remains attached, because the transfer of property subsequent to the attachment of a lien does not affect the lien. *Blacklock* v. *United States*, 208 U. S. 75; *United States* v. *Snyder*, 149 U. S. 210. For "it is of the very nature and essence of a lien, that no matter into whose hands the property goes, it passes *cum onere*; if this were

not the case, it would cease to be a lien." *Burton* v. *Smith,* 13 Pet. 464, 483; *Michigan* v. *United States,* 317 U. S. 338. Therefore, the surrender values merge in the proceeds with the lien attached, and the lien remains enforceable. Two Courts of Appeals have so held. *United States* v. *Behrens,* 230 F. 2d 504 (C. A. 2), certiorari denied, 351 U. S. 919; *United States* v. *Hoper,* 242 F. 2d 468 (C. A. 7).

Similarly, the lien equally attached to the entire proceeds on the same basis as we urged that the beneficiary was the transferee of the proceeds of the policy as well as the cash surrender value. It is to be noted that under the Internal Revenue Code the lien attaches not only on the "property" but also the "rights to property" of the taxpayer. The right reserved by the insured to name his estate as the beneficiary of his insurance results in the proceeds being his assets subject to the lien.[2]

The courts which have held that state law governs transferee liability, absent a federal statute, have also held that, where a federal tax lien has arisen before insured's death, the federal lien statute comes into play and the state statute must give way. *United*

---

[2] In *United States* v. *Metropolitan Life Ins. Co.*, decided January 14, 1958 (C. A. 4), the court said (Slip op. 11) that when the insured's interest in insurance policies is subjected to the tax lien by levy upon the insurance company, this amounts to a seizure of such interest by the United States, and the United States, by virtue of such seizure, may exercise any right which the insured might have exercised under the policies.

States v. *Behrens*, 130 F. Supp. 93 (E. D. N. Y.), affirmed, 230 F. 2d 504 (C. A. 2), certiorari denied, 351 U. S. 919; see *United States* v. *Hoper*, *supra*.[3] This Court and others have upheld the supremacy of the federal lien against all sorts of attempts to impair it by reliance on state statute or court decision. Cf. *United States* v. *Snyder*, *supra*; *Michigan* v. *United States*, *supra*; *United States* v. *Scovil*, 348 U. S. 218; *United States* v. *City of Greenville*, 118 F. 2d 963 (C. A. 4); *United States* v. *Dallas Nat. Bank*, 152 F. 2d 582 (C. A. 5); *United States* v. *Heffron*, 158 F. 2d 657 (C. A. 9), certiorari denied, 331 U. S. 831; *Matter of Rosenberg*, 269 N. Y. 247, certiorari denied *sub nom. Rosenberg* v. *United States*, 298 U. S. 669. In *United States* v. *City of New Britain*, 347 U. S. 81, 84, the Court said: "Obviously, the State cannot on behalf of the City impair the standing of the federal liens, without the consent of Congress." More specifically, the courts have invariably held that state statutes exempting insurance cannot prevail in the face of the supremacy of the federal lien. *Kyle* v. *McGuirk*, 82 F. 2d 212 (C. A. 3); *Cannon* v. *Nicholas*, 80 F. 2d 934 (C. A. 10); *Knox* v. *Great West Life Assur. Co.*, 109 F. Supp. 207 (E. D. Mich.), affirmed

[3] A lien may also be important because it is enforceable without regard to the solvency or insolvency of the transferor of the property, whereas transferee liability presupposes insolvency on the part of the transferor following the transfer. *United States* v. *Hoper*, 242 F. 2d 468 (C. A. 7). This particular distinction need not be considered here, however, because the decedent's estate was in fact insolvent following the transfer (R. 5, 22).

per curiam, 212 F. 2d 784 (C. A. 6); *Fried* v. *New York Life Insurance Co.*, 241 F. 2d 504 (C. A. 2), certiorari denied *sub nom. Fried* v. *United States*, 354 U. S. 922; *Smith* v. *Donnelly*, 65 F. Supp. 415 (E. D. La.).

CONCLUSION

With respect to the petition of the United States (No. 395), the judgment of the Court of Appeals should be reversed. With respect to the cross-petition of Molly G. Bess (No. 410), the judgment of the Court of Appeals should be affirmed.

Respectfully submitted,

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1957.

No. 410.

MOLLY G. BESS, PETITIONER,

vs.

UNITED STATES OF AMERICA.

No. 395.

UNITED STATES OF AMERICA, PETITIONER,

vs.

MOLLY G. BESS.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR MOLLY G. BESS, CROSS-PETITIONER IN NO. 410 AND RESPONDENT IN NO. 395.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1957.

No. 410.

MOLLY G. BESS,

Petitioner,

vs.

UNITED STATES OF AMERICA.

No. 395.

UNITED STATES OF AMERICA,

Petitioner,

vs.

MOLLY G. BESS.

BRIEF FOR MOLLY G. BESS, CROSS-PETITIONER IN NO. 410 AND RESPONDENT IN NO. 395.

Opinions Below.

The opinion of the Court of Appeals (R. 17-22) is reported in 243 F. 2d 675. The opinion of the District Court (R. 10-16) is reported in 134 F. Supp. 467.

Jurisdiction.

The judgment of the Court below (R. 23) was entered March 28, 1957. Rehearing was denied (R. 28) May 20, 1957. On August 9, 1957, by order of Mr. Justice William J. Brennan, Jr., the time within which to file petition for a writ of certiorari was extended to September 19, 1957 (R. 31). The cross-petition was filed on August 22, 1957, and was granted October 28, 1957 (R. 31). The jurisdiction of this Court is invoked under 28 U. S. C. 1254.

Questions Presented.

Herman Bess, deceased husband of the petitioner, was indebted to the United States for Federal income taxes. The assets of his estate were insufficient to pay the income tax debt in full. His life was insured under several life insurance policies over which, at the time of his death, he had the right to change the beneficiary, to borrow against the cash surrender values and the right of assignment. The petitioner, having been named as beneficiary when the policies were taken out, collected the proceeds when the policies matured at death of the insured. Herman Bess was solvent at all times when he paid the insurance premiums. There was no fraud against creditors in taking out the insurance, in naming the petitioner as beneficiary, nor in paying the premiums, nor did any such act render Herman Bess insolvent.

1. The question presented in No. 395 and No. 410 is whether the cross-petitioner, Molly G. Bess, is liable either

in law or in equity for the unpaid income tax debt of her deceased husband, Herman Bess, to the extent of any part of the proceeds paid to her as beneficiary of insurance policies on his life, the premiums for which he paid when he was solvent and without fraud of creditors.

Statutes Involved.

SEC. 3670. PROPERTY SUBJECT TO LIEN.

If any person liable to pay any tax neglects or refuses to pay the same after demand, the amount (including any interest, penalty, additional amount, or addition to such tax, together with any costs that may accrue in addition thereto) shall be a lien in favor of the United States upon all property and rights to property, whether real or personal, belonging to such person (53 Stat. 448, 26 U. S. C. 1952 ed., sec. 3670).

SEC. 1652. CIVIL PROCEDURE ACT.

The laws of the several states, except where the Constitution or Treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply (62 Stat. 944, 28 U. S. C. Sec. 1652).

New Jersey R. S. 17:34-28. BENEFICIARY'S RIGHT TO PROCEEDS.

When a policy of insurance is effected by any person on his own life, or on another life in favor of a person other than himself having an insurable interest therein, the lawful beneficiary thereof, other than himself or his

legal representatives, shall be entitled to its proceeds, against the creditors and representatives of the person effecting it. The person to whom a policy of life insurance is made payable may maintain an action thereon in his own name. Subject to the statute of limitations, the amount of any premiums for the insurance paid in fraud of creditors, with interest thereon, shall, however, inure to their benefit from the proceeds of the policy; but the company issuing the policy shall be discharged of all liability thereon by payment of its proceeds in accordance with its terms, unless, before the payment, the company shall have written notice by or in behalf of some creditor, with specification of the amount claimed, claiming to recover for certain premiums paid in fraud of creditors.

Source. L. 1902, c. 134, Sect. 38, p. 422 (C. S. p. 2850, Sect. 38).

New Jersey R. S. 17:34-29. Policies to Inure to Benefit of Married Woman.

Every policy of life insurance made payable to or for the benefit of a married woman, or after its issue assigned, transferred or in any way made payable to a married woman, or to any person in trust for her or for her benefit, whether procured by herself, her husband or by another person, and whether the assignment or transfer is made by her husband or by another person, shall inure to her separate use and benefit, and to that of her children, according to the terms and provisions of the policy or assignment, subject to the foregoing provisions relating to premiums paid in fraud of creditors.

Source. L. 1902, c. 134, Sect. 39, p. 422 (C. S. p. 2850, Sect. 39).

Statement.

1. *Nature of the action.*—This action was instituted by complaint filed in the United States District Court, District of New Jersey, by the United States of America, as plaintiff, against Molly G. Bess, as defendant, who is hereinafter referred to as cross-petitioner. The complaint alleged that the cross-petitioner was a transferee of property of Herman Bess, deceased, by virtue of having been beneficiary of his life insurance, and thus liable, at law or in equity, for the unpaid income tax owing by said Herman Bess, deceased.

No action was taken by the Commissioner of Internal Revenue to assess the transferee liability against the cross-petitioner, Molly G. Bess, under the provisions of Section 311 of the Internal Revenue Code of 1939 (R. 10, par. 31).

2. *The facts.*—The case was tried on a stipulation of facts (R. 3-10).

Cross-petitioner, Molly G. Bess, is the widow of Herman Bess, a resident of New Jersey, who died June 29, 1950. At the time of his death, there were in effect nine life insurance policies on the life of Herman Bess, in one of which his estate was named as beneficiary and in eight of which the cross-petitioner was named as beneficiary. The cross-petitioner was designated as the beneficiary of such policies when they were issued and remained continuously as such beneficiary until the insured's death, except for immaterial, temporary changes respecting two policies (R. 6-9, Opinion; R. 17, 18). Seven of such policies were issued during 1934, 1935, 1936 and 1937. The eighth, a group insurance policy

with no cash value, was issued June 19, 1950 (R. 6-9, Opinion, R. 17, 18).

Herman Bess retained the right to change the beneficiary of the policies and also retained the right to borrow upon the security of the cash surrender value of the seven policies described first herein (Opinion, R. 17, and R. 6-9, pars. 18-28).

Herman Bess paid all of the premiums until his death out of his own funds. He was solvent, at all times, when such premiums were paid (R. 9, par. 30).

At the time of his death Herman Bess owned in joint tenancy with the cross-petitioner, his wife, real estate with a net equity value of $52,054.48, and personal property with a value of $3,187.15 (R. 6, par. 17). In addition, Herman Bess owned other assets which became part of his estate (R. 5, par. 11). His estate also collected the proceeds of the ninth life insurance policy in which his estate was designated as beneficiary (R. 6-7, par. 19).

On July 17, 1952 the Monmouth County Court, Probate Division, adjudged the estate of Herman Bess as insolvent (R. 5, par. 12).

After paying the funeral and administration expenses all of the remaining assets of the estate were applied toward payment of income tax balances assessed against Herman Bess. After crediting such payments there remained due, on account of such taxes, a total of $8,874.57, reflecting balances of $4,159.31 for 1945, $3,789.32 for 1946 and $925.94 for 1947 (R. 11), the entire balances owing for 1948 and 1949 having been paid in full, and the balance for 1945 having been reduced.

3. *The District Court decision.*—The learned Trial Judge concluded that *Pearlman* v. *Commissioner,* 153 Fed. 2d 560, 3 Cir., laid down a broad policy imposing transferee liability upon a life insurance beneficiary to the full extent of the life insurance proceeds, without regard to the provisions of State Law, and with no particular significance attached to the solvency or insolvency of the deceased taxpayer. On the basis of the *Pearlman* decision, which the learned Judge decided was controlling here, he rendered judgment against the cross-petitioner in the amount of $11,657.30 (Opinion, R. 14, 15; Judgment, R. 16).

4. *The Court of Appeals decision.*—The Court decided that the cross-petitioner was not a transferee of the proceeds of the policies (Opinion, R. 21).

Holding, however, that "since there was a Federal tax question to be decided it should be decided on general law as laid down by the Federal courts and not be subject to the limitation in the law of any state" (Opinion, R. 19), the Court decided that Herman Bess was insolvent at the time of his death, and that the cross-petitioner was liable as a transferee of $3,362.53, the cash surrender or loan value of the insurance policies at the time of death (Opinion, R. 22).

In footnote 2 (Opinion, R. 19, 20) the Court indicated that the cross-petitioner is not liable to any extent if the New Jersey law is applicable.

Summary of Argument.

I.

The Transferee Theory.

On the facts of this case the cross-petitioner is not under any liability to the United States as transferee of Herman Bess whether the decision is made under general law laid down by the Federal Courts, as the Court below decided, or under State law, as the cross-petitioner urges.

The question in the case at bar should be decided under the law of New Jersey because:

(1) Title 28, Section 1652, U. S. C. provides, and this Court in *Erie R. Co.* v. *Tompkins*, 304 U. S. 64*, held that the laws of the several states, except where the Constitution or Treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the Courts of the United States, in cases where they apply.

(2) No section of the Federal Revenue Act which might apply to the case at bar defines the standards to be applied, the terms used, or the property which they affect. An inquiry into State law is inescapeable in order to determine the application of the Federal Revenue Act when that Act fails to provide its own definition, *Helvering* v. *Fuller*, 310 U. S. 69, 74; *Morgan* v. *Commissioner*, 309 U. S. 78 and other cases cited in the argument.

(a) In footnote 3 of its opinion (Opinion, R. 19) the Court below correctly stated that if the law of New Jersey is applied then the cross-petitioner is under no liability to the United States. The basis for such a decision, if New

* The *Erie* doctrine would appear to be applicable whenever state created rights are in issue regardless of basis for federal jurisdiction. 62 Harvard Law Rev. 1030, 1031, footnote 6.

Jersey law is applicable, is the New Jersey Statute, namely, N. J. Revised Statutes, Sections 17:34-28 and 17:34-29 and the decisional law of the New Jersey Courts.

(b) The Court below has not correctly applied the general law as laid down by the Federal Courts, and particularly as laid down by this Court in *Central Bank of Washington* v. *Hume*, 128 U. S. 195 (1888). The *Hume* case laid down the rule that actual fraud must be established as the basis for recovery from a wife-beneficiary since fraud will not be imputed to a married man from the mere fact of payment, at a time when he is insolvent, for life insurance taken out to protect his wife and children. The reason for the rule is that public policy imposes a legal obligation upon a married man to provide against the destitution of his wife and children. Whether the test laid down in the *Hume* case is applied, with respect to premium payments, as of the time of such payments as this Court held in *Hume*, or is applied, with respect to cash surrender value, as of the time of death as the Court below held in the case at bar, the cross-petitioner is under no liability because there is no allegation, evidence nor hint of fraud on the part of either Herman Bess or the cross-petitioner at any time. Furthermore, the stipulation admits that Herman Bess was solvent at all times when premiums were paid (R. 9, par. 30). It is urged that Herman Bess was also solvent at the time of his death, although the Court below inferred that he was insolvent (Opinion, R. 22), because in addition to his substantial property interests (R. 5, par. 11 and R. 6, par. 17), he also had substantial amounts of income as reflected by the income taxes.

II.

The Tax Lien Theory.

2. The tax lien theory, under Section 3670 Internal Revenue Code of 1939, which the Government in its petition for certiorari reserved the right to assert as an alternative basis for recovery (Pet. for cert., No. 395, footnote 2, p. 4), should not be entertained as a basis for recovery on appeal because it was not asserted as a basis for recovery before the Trial Court; and especially because the case was submitted for decision to the Trial Court on a stipulation of facts which was, in good faith, drafted to present facts relevant to the issue presented for decision. See *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 (1935).

3. Moreover, the Government is not entitled to recover on the merits of the lien theory.

In the first place, it has not been established that the taxpayer, Herman Bess, neglected or refused to pay his tax, which the statute imposes as conditions precedent to the creation of the statutory lien. On the contrary, the stipulation admits that the taxpayer, Herman Bess, until his death made periodic payments on account of the tax. Therefore, the facts establish that the taxpayer was acting in good faith, and was neither neglecting nor refusing to pay the tax.

4. In the second place, the beneficiary is entitled to the proceeds, even to the exclusion of an assignee of the policy, under the decisional law of New Jersey, which is applicable because the lien statute does not define the property or rights to property to which the lien may attach. See *Anderson* v. *Broad St. National Bank*, 90 N. J. Eq. 78, affirmed 91 N. J. Eq. 331, and others cited in the argument.[1]

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[1] Cf. *Poe* v. *Seaborn*, 282 U. S. 101, 118; *Morgan* v. *Commissioner*, 309 U. S. 78; *Helvering* v. *Fuller*, 310 U. S. 69, 74.

III.

The Amount of Liability.

5. If the Court decides the basic issue of liability in favor of the cross-petitioner then the question raised in No. 395 with respect to the amount of the liability need not be considered.

However, if it is decided that the cross-petitioner is under liability as a transferee, the amount of such liability is limited to the value of the transferred property. *Voss* v. *Wiseman*, 234 F. (2d) 237 (10 Cir. 1956); *Borg* v. *McCroskery*, 120 N. J. Eq. 80, 86 (1936).

Since the proceeds were not, and never could be, the property of Herman Bess, the proceeds were not property transferred by Herman Bess to the cross-petitioner, and the Court below so decided (Opinion, R. 21). This finding accords with *U. S.* v. *New*, 217 F. (2d) 166 (7 Cir. 1954) and *U. S.* v. *Truax*, 223 F. (2d) 229 (5 Cir. 1955).

The Court below decided that cash surrender value of the policies was the item of property which was transferred to the cross-petitioner (Opinion, R. 22). It is urged that in no event does the transfer consist of more than the premiums or the cash surrender value, and liability, if it properly exists on account of such a transfer, is limited to the premium payments or cash surrender value.

ARGUMENT.

POINT 1.

The wife of an insured debtor, who as beneficiary collects on husband's life insurance, is not liable to her husband's creditors as a transferee of property of her husband, in the absence of fraud, either

(a) Under the law of New Jersey, or

(b) Under general law as laid down by the Federal Courts.

The Court below decided that the question of liability in this case is to be answered without referring to state law.

The cross-petitioner urges that whether she is a transferee and whether, and to what extent, she is liable as such a transferee is a question to be decided in accordance with the law of New Jersey where she and the alleged transferor resided.

With the exception of the Court below, all other Courts of Appeal which have decided the question hold that State rather than Federal law determines the substantive liability in transferee cases.[2] This Court, in *Philips* v. *Commissioner*, 283 U. S. 589, 602, reserved the question.

With respect to the transferee theory the Government has not invoked any section of the Federal statutes. Paragraph 31 of the Stipulation (R. 10) admits that no transferee assessment under Section 311 of the Internal Revenue Code of 1939 was proposed against the cross-petitioner.

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[2] *Tyson* v. *Commissioner*, 212 F. (2d) 16 (6 Cir.); *Rowen* v. *Commissioner*, 215 F. (2d) 641 (2 Cir.); *U. S.* v. *Neic*, 217 F. (2d) 166 (7 Cir.); *U. S.* v. *Truax*, 223 F. (2d) 229 (5 Cir.); *Stern* v. *Commissioner*, 242 F. (2d) 322 (6 Cir.).

The Civil Procedure Act, 62 Stat. 944, 28 U. S. C. Section 1652 (formerly Section 34, of Rules of Decision Act of 1789, 1 Stat. 92), provides:

> "The laws of the several states, except where the Constitution or Treaties of the United States or Acts of Congress otherwise require or provide, shall be regarded as rules of decision in civil actions in the courts of the United States, in cases where they apply.".

Referring to Section 34 of the Federal Judiciary Act of 1789, the predecessor to the present statute quoted above, Justice Brandeis in his opinion for this Court in *Erie R. Co.* v. *Tompkins*, 304 U. S. 64, 72 (1938), quoted with approval from an earlier decision of this Court as follows:

> "The statute, however, is merely declarative of the rule which would exist in the absence of the statute." *Mason* v. *U. S.*, 260 U. S. 545, 559.

There is no privity, in this case, between the United States of America and the cross-petitioner, based either upon a statute, contract, or other direct relationship. The alleged claim against the cross-petitioner is derivative, since it is based upon the fact that the United States is a creditor of Herman Bess. Regardless of the origin of the debt, with respect to the cross-petitioner the United States has no greater rights than any private creditor of Herman Bess might have under the same circumstances. To hold otherwise, would clothe the Government with rights and privileges not conferred upon it by the Constitution. In *U. S.* v. *Scott*, 167 F. (2d) 301, 8 Cir. (1948), the Court ruled that an action by the United States against a third party to recover for taxes owed by a taxpayer, as against the

third party, is for collection of a debt rather than collection of taxes, and held that the liability should be determined in accordance with State rather than Federal statutes.

Furthermore, as the Court pointed out in *Rowen v. Commissioner*, 215 F. (2d) 641, 2 Cir., the question of liability even under Section 311 of the Internal Revenue Code, should be determined in accordance with the law of the applicable state because that statute does not define how the liability shall be determined.

In its prior arguments the Government has contended that a trust was impressed upon the property of Herman Bess which followed into the proceeds of the life insurance policies. No basis, nor authority, can be found for holding that such a trust is imposed upon the proceeds. Certainly, an implied constructive trust can arise only with respect to money stolen or otherwise wrongfully obtained by the transferor, who never acquired title and therefore could not transfer title. Nor can there be a resulting trust, since there was no intention on the part of Herman Bess, that the proceeds of the life insurance be held for the benefit of himself or his creditors.

Glenn, in Fraudulent Conveyances and Preferences wrote concerning creditor's rights in life insurance proceeds:

> "The creditor, * * *, is not like the cestui que trust who traces misappropriated funds for the reason that, as we have seen, a debtor does not hold his testate in trust for creditors. If a trustee pays premiums out of misappropriated trust funds, the beneficiary may take over the policy itself. But the creditor who shows that payment of a premium was a fraudulent conveyance is entitled only to a return

of what his debtor transferred, and so his claim is limited by that amount. This seems to be the sound view and it is supported by good authority." Glenn, Fraudulent Conveyances and Preferences, Revised Ed., vol. 1, section 178, p. 323. See also *Shaler* v. *Trowbridge*, 28 N. J. Eq. 595 (E. & A. 1877), in which a constructive trust was imposed upon insurance acquired with embezzled funds.

(a) New Jersey law.

A wife-beneficiary of life insurance on her husband's life is not liable for her husband's debt, as a transferee of his property, in the absence of fraud, under New Jersey law.

In footnote No. 3 to the Opinion (opinion, R. 13), the Court below correctly stated that no liability attached to the cross-petitioner if New Jersey law is applicable.

The applicable law of the State of New Jersey is contained in Sections 28 and 29, Chapter 34, Title 17 of the New Jersey Revised Statutes, *supra*, pages 3, 4 of this brief, and the decisions of the New Jersey courts which have construed the statute.[3]

The Court below, however, ruled that the question in this case is one to be answered without referring to State law limitations. The Court below may have accepted the view urged by the Government that the New Jersey statute is an exemption statute, and is not to be applied against the Government. In stating its view the Court below referred to its prior decision in *Pearlman* v. *Commissioner*, 153 F. (2d) 560 in which the Pennsylvania statute which exempts

[3] *Sullivan* v. *Maroney*, 76 N. J. Eq. 104, 109, 73 A. 843, 844 (1909); *Borg* v. *McCroskery*, 129 N. J. Eq. 80, 184 A. 187.

the entire proceeds, was involved. Unlike the Pennsylvania statute, which exempts the entire proceeds, the New Jersey statute provides a logical rule for marshalling the proceeds between the beneficiary and creditors in accordance with the rule established by this Court in *Central Bank of Washington* v. *Hume*, 128 U. S. 195 (1888). The New Jersey statute was first adopted in 1896, within one year after the Court of Chancery in *Merchants' & Miners' Transportation Co.* v. *Borland*, 53 N. J. Eq. 282 (1895), disagreed with the rule of the *Hume* case. Within one year after the decision in *Merchants' & Miners' Transportation Co.* v. *Borland*, *supra* "and probably because of it, the Legislature passed P. L. 1896, p. 240, to declare rights as between an insured's creditors and his beneficiary * * * and that statute was incorporated as part of the Insurance Act of 1902 (Comp. Stat. p. 2836) * * * " (now R. S. 17:34-28 and 17:34-29). Quotation taken from *Borg* v. *McCroskery*, 120 N. J. Eq. 80, 83, 84.[4]

(b) General law as laid down by the Federal Courts.

If the question is to be decided in accordance with general law as laid down by the Federal Courts, as the Court below concluded, then the rule laid down by this Court in *Central Bank of Washington* v. *Hume*, 128 U. S. 195 (1888), is expressive of such general law, and is controlling.

In the *Hume* case, this Court, basing its decision upon sound public policy, enunciated a rule which, at the time, some criticized as a variation from the traditional interpretation of a creditor's right to reach a fraudulent convey-

[4] See also, Glenn, Fraudulent Conveyances and Preferences, revised ed., vol. I section 177, p. 322, and Vance, Insurance (2d ed.) p. 624.

ance.[5] However, the social policy was sound and the rule responded to public need. It was soon followed by State Courts, and adopted by Legislatures in various states so that the rule of the *Hume* case has become the majority view, cf. "Fraudulent Conveyances", 25 Virginia Law Review, 588, 593 (1939).

In the *Hume* case a creditor sought to reach proceeds of the debtor's life insurance collected by the debtor's wife as the beneficiary. Pointing out that it is the fraudulent intent of the donor which vitiates a transfer and that such fraudulent intent is conclusively presumed if the donor is actually insolvent the Court wrote (*Central Bank of Washington* v. *Hume*, 128 U. S. 195):

> "But the circumstances of each particular case should be considered, as in Patridge *v.* Gopp, 1 Eden, 163, Amb. 596, where the Lord Keeper, while holding that debts must be paid before gifts are made, and debtors must be just before they are generous, admitted that the fraudulent intent might be collected from the magnitude and value of the 'gift' ". 128 U. S. 195, 211.

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Deciding how to apply the rule so stated, to life insurance, the Court, in the *Hume* case wrote:

> "It seems to us that the same public policy which * * * recognizes the support of wife and children as a positive obligation in law as well as morals, should be extended to protect them from destitution after the debtor's death, by permitting him, not to accumulate a fund as a permanent provision, but to devote a moderate portion of his earnings to keep on foot a security for support already, or which could thereby

[5] Williston, American Law Review, volume 25, p. 185; *Merchants' & Miners' Transportation Co.* v. *Borland*, 53 N. J. Eq. 282.

be lawfully obtained, at least to the extent of requiring that, under such circumstances, the fraudulent intent of both parties to the transaction should be made out." 128 U. S. 195, 211, 212.

The Court in the *Hume* case recognized the payment of premiums as the time and subject of the transfer. Some courts have decided that a transfer occurs at the time when an insured changes the beneficiary from the executors of his estate to some other person. *Rowey* v. *Commissioner*, 215 F. (2d) 641, 2 Cir. (1954); *Pearlman* v. *Commissioner*, 4 T. C. 34.

In the instant case, the Court below decided that a transfer of the cash surrender value occurred at the moment of death.

It is respectfully urged that termination of the insured's control of the policy, as the result of his death, is not that affirmative act of transfer contemplated as the basis for recovery by a creditor.

Those cases which involve the imposition of the Federal Estate Tax are not apposite since the estate tax applies not only with respect to property transferred at death but also with respect to property control over which is terminated at death. *Chase Nat. Bank* v. *United States*, 278 U. S. 327, see also section 811 (f), Internal Revenue Code of 1939, respecting property subject to power of appointment.

The stipulation admits that Herman Bess was solvent at all times when he paid premiums (R. 9, par. 30). At the time of his death he owned in joint tenancy with the cross-petitioner, his wife, real estate with a net equity value of $52,054.48, and personal property with a value of $3,187.15 (R. 6, par. 17). He also owned other assets (R. 5, par. 11).

In addition it can be inferred from the size of his income taxes that he also earned substantial income. From July 30, 1948 until his death, by virtue of periodic payments, he reduced his back taxes by $6,800.41 (R. 4, par. 5). There has been no allegation, evidence nor hint of fraud at any time. Under those circumstances, applying the rule of law laid down in *Central Bank of Washington* v. *Hume*, 128 U. S. 195, there has been no fraudulent transfer, either of the premiums when paid, or the cash surrender value at death, which the Government can recover from the cross-petitioner.

POINT 2.

The Government cannot on appeal properly assert as an alternative basis for recovery, a basis for recovery which was not raised in the pleadings nor presented to the trial Court.

In its petition for certiorari, No. 395, the Government reserved the right to assert as an alternative basis for recovery that a lien, pursuant to Section 3670 Internal Revenue Code, of 1939, attached to the property of Herman Bess, and that this was a proceeding to enforce the lien.

The "tax lien theory" was not asserted in the Complaint which initiated this proceeding, nor in any other pleadings before the trial Court. It was not presented to, considered by nor ruled upon by the trial Court. Therefore it is urged that this question should not be entertained, or considered as a basis for decision by this Court, especially because the case was submitted for decision to the trial Court on a stipulation of facts which was, in good faith,

drafted to present the facts relevant to the issue presented for decision. See *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200 (1935).

POINT 3.

No lien arose under Section 3670, since the facts do not establish the statutory prerequisites, namely, neglect or refusal of the taxpayer to pay the tax.

The lien under Section 3670 is predicated upon a condition precedent, namely, "If any person liable to pay any tax neglects or refuses to pay the same after demand * * *".

Had Congress intended to create a lien based upon the mere fact of a tax debt, standing unpaid by itself, it would not have used the conditional "if" followed by the definition of the circumstances, namely, neglect or refusal to pay, upon which the condition turns.

"Neglect" is defined in Funk & Wagnalls Practical Standard Dictionary as follows:

> "Neglect. 1. To fail to treat with attention.
>
> 2. To ignore.
>
> 3. To fail to perform through carelessness or oversight."

"Refuse" is defined in Funk & Wagnalls Practical Standard Dictionary as follows:

> "Refuse. 1. To decline to do, permit, or yield.
>
> 2. To reject; deny; repel."

Cross-petitioner invites the Court's attention to the pertinent language found in the recent opinion, *In the matter of Clinton Crockett, etc.*, 150 F. Supp. 352 (1957):

> "In order for the lien of Sec. 3670 (I. R. C. 1939) to attach to the individual property of the bankrupt, it must be established that (1) he is a 'person liable to pay' the tax, and (2) he has 'neglected or refused to pay the same after demand'." 150 F. Supp. 352, 354.

And:

> "(5) It cannot be determined, however, on the record now before this Court, whether petitioner has perfected the lien it asserts against the bankrupt's property. By the plain wording of Sec. 3670, *supra*, the lien does not attach unless and until the delinquent taxpayer 'neglects or refuses to pay the same after demand'. It is incumbent upon petitioner to show that these statutory prerequisites have been fulfilled before the Referee can treat petitioner as a lien creditor." 150 F. Supp. 352, 354.

The Government has the burden of affirmatively establishing the existence of neglect or refusal as a prerequisite to the arising of the lien, under the clear language of the statute. Not only has the Government failed to establish either "neglect" or "refusal" to pay, but it is suggested that the fact of the periodic payments, amounting to $6,800.41, made by Herman Bess, after simultaneous assessment and demand respecting the 1945 and 1946 taxes (R. 4, pars. 5 and 6), until his death as admitted in paragraph 5 of the Stipulation (R. 4) can only serve to establish that he was complying in good faith, and probably with the consent of the Collector of Internal Revenue both as to the amounts and manner of payment. 1947 tax was assessed after date of his death (R. 5, par. 8).

POINT 4.

No lien in favor of the Government has attached to, nor followed into the insurance proceeds.

Whether the Government, when it has properly established that a lien arose under Section 3670 against an insured taxpayer, can collect the amount of its lien, after the taxpayer's death, from the beneficiary of the life insurance presents a question not previously decided by this Court. The question was decided favorably to the Government in *U. S.* v. *Behrens*, 230 F. (2d) 504, 2 Cir., affg. 130 F. Supp. 93, cert. den. 351 U. S. 919, and was followed by *U. S.* v. *Hoper*, 242 F. (2d) 468, 7 Cir., reversing 144 F. Supp. 281. Those cases involved residents of New York and Illinois, respectively. In order to develop this argument; in what is believed to be logical order, comment respecting the *Behrens* and *Hoper* cases is withheld at this point, and is taken up on page 27 of this brief.

It is urged, as indicated by the argument which follows, that the property rights to which the statutory lien attaches are to be determined in accordance with the law of the applicable State. In the instant proceeding, the applicable State law is that of New Jersey. If the law of New Jersey is applied, as the cross-petitioner urges is required, then the Government cannot recover from the cross-petitioner under the lien of Section 3670.

Section 3670 provides a lien, when the conditions precedent are established, "upon all property and rights to property whether real or personal". Neither that section nor any other defines the terms "property and rights to property."

The rule is well established that where the Revenue Act does not define the property and interest in property to which it is intended to apply, the meaning of the words must be determined pursuant to the law of the applicable State.

In the application of the income tax law this Court has held that rights to and ownership of property should be decided in accordance with state law. When the Revenue Act provides no definition, resort to State law is inescapable. *Helvering* v. *Fuller*, 310 U. S. 69, 74.[6]

In *U. S.* v. *Penn Mutual Life Insurance Co.*, 3 Cir., 130 F. (2d) 495 and *Karno-Smith Co.* v. *Maloney*, 3 Cir., 112 F. (2d) 690, it was held that property rights are to be determined in accordance with State law even where the United States or the Collector of Internal Revenue seeks to assert its tax lien. Cf. also *Cannon* v. *Nicholas*, 10 Cir., 80 F. (2d) 934, 936 (1935).

The insurance policy is a contract. The law of the State is as much a part of the contract as if it were incorporated into the insurance policy itself, *Central Bank of Washington* v. *Hume*, 128 U. S. 195. It follows, then, that all parties to the contract, including a lienor who claims derivatively by virtue of a lien against the insured, are governed by and have only those rights and property interests which are conferred under the provisions of the contract as interpreted by the law of the State.

The Courts of New Jersey have continuously held, in a long line of cases, that an individual who is designated as a beneficiary in a policy of insurance holds a property

[6] See, *Freuler* v. *Helvering*, 291 U. S. 35; *Blair* v. *Commissioner*, 300 U. S. 5; *Poe* v. *Seaborn*, 282 U. S. 101.

right which can only be divested by making a change of beneficiary in the manner provided by the policy contract and that the beneficiary takes the proceeds even to the exclusion of the assignee-owner of the policy if death occurs before the beneficiary is changed,[7] on the premise that the respective rights of the parties are governed by the intention as expressed in the policy contract.

Other states also subscribe to the same rule.[8] Some states hold to the contrary on the premise that when an insured assigns the policy he intends that the assignee shall receive the proceeds.[9]

In *Anderson* v. *Broad St. National Bank*, 90 N. J. Eq. 78, affirmed, 91 N. J. Eq. 331, the insured having reserved the right to change the beneficiary, and the right to assign the policy, made an assignment of the policy to a bank as security for a loan. The insured's wife was beneficiary of the insurance policy prior to its assignment of the bank. No change of beneficiary was thereafter made. The question before the Court was whether the wife, as beneficiary, or the bank, as assignee, of the policy was entitled to the proceeds. Holding that the assignment of the policy did

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[7] *Metropolitan Life Insurance Co.* v. *Woolf* (New Jersey Court of Errors and Appeals 1946), 138 N. J. Eq. 450, 47 A. 2d 340; *Metropolitan Life Insurance Co.* v. *Clanton*, 76 N. J. Eq. 4, 73 A. 1052; *Sullivan* v. *Maroney*, 76 N. J. Eq. 104, 73 A. 842, affirmed 77 N. J. Eq. 565, 78 A. 150; *Anderson* v. *Broad Street National Bank*, 90 N. J. Eq. 78, 105 A. 599, affirmed 91 N. J. Eq. 331; *Union Central Life Insurance Co.* v. *Elizabeth Trust*, 119 N. J. Eq. 505, 183 A. 181; *Prudential Insurance Co.* v. *Mantz*, 128 N. J. Eq. 480, 486.

[8] *Muller* v. *Penn. Mutual Life Ins. Co.*, 62 Colo. 245, 161 Pac. 148 (1916); *Johnson* v. *New York Life Ins. Co.*, 56 Colo. 178, 138 Pac. 414 (1913); *Shum* v. *Lawrenceburg Nat. Bank*, 314 Ky. 297, 234 S. W. 2d 962 (1950); *Douglas* v. *Equitable Life Assur. Soc.*, 150 La. 519, 90 So. 834 (1922); *Citizen's Bank* v. *Knight*, 15 La. App. 62, 130 So. 270 (1930); *Finnegan* v. *Prudential Ins. Co.*, 300 Mass. 147, 14 N. E. 2d 172 (1938); *Goldman* v. *Moggs*, 287 Mass. 393, 191 N. E. 873 (1934).

[9] *Equitable Life* v. *Mitchell*, 248 Ill. app. 401 (1927); *Davis* v. *Modern Ind. Bank*, 279 N. Y. 405, 18 N. E. 2d 639 (1939); *Cummins Estate*, 200 Misc. 467, 105 N. Y. S. 2d 104 (1951).

not divest the interest of the beneficiary, the learned Vice Chancellor wrote:

> "After a careful examination of the authorities, I am of the opinion that whether the interest be regarded as vested and defeasible, contingent, a mere expectancy, or whatever the characterization may be, if the policy stipulates the course by which the beneficiary's interest is to be nullified, he cannot be deprived of his right unless the prescribed mode for its destruction is followed, and that the assignment in this case by the assured had not that effect." *Anderson* v. *Broad St. National Bank*, 90 N. J. Eq. 78, 82.

It has been held that unless the insured has exercised his option to surrender the policy for cancellation, there is no money owing to him, and there is no fund to which the statutory lien can attach, *U. S.* v. *Metropolitan Life Ins. Co.*, 2 Cir., 130 F. (2d) 149 (1942) and *U. S.* v. *Penn Mut. Life Ins. Co.*, 3 Cir., 130 F. (2d) 495 (1942).

Vance, in his treatise on insurance, has written:

> "It may be said that, as a general rule, the policy is not to be regarded as liable to seizure under any form of judicial process against the insured so long as the duty of the insurer to pay is subject to any contingency, or to any condition precedent. Such condition may be under the control of the insurer, as where the policy gives to the insurer the power to elect between several optional forms of settlement; or where it permits the insured to fix the debt of the insurer by electing to receive cash, or a paid-up policy, or some other optional benefit. Until such option is exercised in favor of a cash payment, the insurer cannot be said to be so indebted to the

> insured as to be subject to garnishment. But where the only condition to the insurer's promise to pay an agreed surrender value is the insured's giving up the policy for cancellation, the Courts generally permit the attaching creditor to deliver up the policy and receive the surrender value." Vance, Insurance (2d Ed.), Section 161, page 615, et seq.

It may be conceded that, in a proper action during the insured's lifetime, the Government can compel the insured to surrender the policy, and thereby recover the cash surrender value, see *U. S.* v. *Roark*, D. C., West. Dist. Mo., So. West. Div., decided 7/17/57, 57-2 USTC No. 9883, *U. S.* v. *Metropolitan Life Ins. Co.*, 2 Cir., 130 F. (2d) 149.

Until recently it has been held that unless the Court could act in personam upon the insured, the Court was powerless to enter judgment against the insurance company for the surrender value when the Government sought to enforce its lien for taxes of the insured. Recently, however, in the case of an absconding taxpayer, who had been convicted of income tax fraud, the Court of Appeals, 4 Cir., directed the insurance company to pay the cash surrender value to the Government, ruling that the judgment of the Court had the effect of relieving the insurance company of its obligation under the insurance contract, see *U. S.* v. *Metropolitan Life Ins. Co.*, 4 Cir., decided 1/14/58, 58-1 USTC No. 9238.

It does not follow, however, that the surrender value can be followed after death of the insured has terminated his option to receive it. In *U. S.* v. *The Penn Mutual Life Ins. Co.*, 3 Cir., 130 F. (2d) 495 (1942), it was held that when the policy lapsed, after distraint for taxes was served upon the insurance company, and extended insurance was

issued, there no longer was any cash surrender value to be recovered by the Government.

In *U. S.* v. *Behrens*, 230 F. (2d) 504, 2 Cir., affirming 103 F. Supp. 93, cert. den. 351 U. S. 919, the Court of Appeals upheld the decision of the District Court for New York that a tax lien arose against an insured taxpayer, under Section 3670, which attached to the cash surrender value and followed into the insurance proceeds. Adopting and following the ruling in *Behrens*, the Court in *U. S.* vs. *Hoper*, 242 F. (2d) 468, 7 Cir., reversed the District Court for Illinois, 144 F. Supp. 281, which disagreed with and refused to follow the ruling in *Behrens*.

The Court of Appeals in the *Behrens* case in its opinion discusses the legal rights with respect to cash surrender value of life insurance policies and concludes:

> "It follows from what we have said that there is no logical escape from holding that the 'surrender value' comes to an end on the insured's death, if we dispose of the controversy in accordance with the ordinary rules governing contracts." 230 F. (2d) 504, 506.

Immediately after the statement above quoted is the following:

> "(3) However, in Rowen *v.* Commissioner, supra (p. 647), we held that 'it is not realistic to view his' the insured's 'death as wiping out these values. Under the policies his death was merely a condition upon which the surrender values no longer payable to the decedent became merged in the greater values which the insurers were obligated to pay the beneficiaries.' There can be no doubt that the courts have spoken of the 'surrender value' as though it were in fact a fund which the insurer held as a custodian for

the insured. This way of looking at the situation was long ago stated by Judge Addison Brown[3] with his customary clarity and the Supreme Court has twice quoted what he said with approval.[4] We shall not requote it in full; it is enough to excerpt the following passages. 'Though this excess of premiums paid is legally the sole property of the company, still in practical effect, though not in law, it is the moneys of the assured deposited with the company in advance to make up the deficiency in later premiums. So long as the policy remains in force, the company has not practically any beneficial interest in it, except as its custodian with the obligation to maintain it unimpaired and suitably invested for the benefit of the insured. This is the practical, though not the legal relation of the company to this fund.' This language obviously treats the surplus of the paid premiums that makes up the 'surrender value', as a 'fund' held for the insured, and, if it were such, the lien would follow it into the 'proceeds'. Regardless of what Judge Medina and I might have held, had the question come up as *res nova*, we think that this interpretation is imperative, and therefore we all agree that the 'proceeds' were subject to the lien.'' (230 F. (2d) 504, 506, 507).

The authorities cited in *Behrens*, namely, Judge Brown's decision in *In re McKinney*, 15 Fed. Rep. 535, 537, *Hiscock* v. *Mertens*, 205 U. S. 202, 211, 212, and *Burlingham* v. *Crouse*, 228 U. S. 459, 469, are bankruptcy cases in which the question presented was whether and to what extent the trustee in bankruptcy acquired the ownership of the cash surrender value of the bankrupt's life insurance.

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[3] *In re M'Kinney*, 15 Fed. Rep. 535, 537.

[4] *Hiscock* v. *Mertens*, 205 U. S. 202, 211, 212; *Burlingham* v. *Crouse*, 228 U. S. 459, 469.

In *McKinney* the facts disclose that the bankrupt actually assigned his policy, which named his executors and assigns as the beneficiary, to the Trustee. The Court held that as a result of the assignment of the policy the trustee became the owner to the extent of the cash surrender value, and was entitled to collect a portion of the proceeds, only to that extent.

The *Hiscock* and *Burlingham* cases arose at a time when the bankruptcy act specifically vested the trustee with ownership of all of the bankrupt's property, but provided that the bankrupt might retain, or re-acquire, his life insurance policies upon paying the cash surrender value to the trustee.

Clearly, then, in all three cases, *McKinney*, *Hiscock* and *Burlingham*, there had been an actual conversion of ownership, of the policy, either by actual assignment as in McKinney or by statutory effect as in *Hiscock* and *Burlingham*.

Actual conversion of ownership might possibly create a trust in favor of the new owner on the theory that it was intended by the act of conversion to benefit the new owner to the extent of the surrender value at time of conversion.

It does not follow, however, that a mere lien, if one arose in the instant case, without conversion into ownership vests the lienor with ownership of the surrender value. Nor, does it follow that a lien upon the insured's contractual right to surrender the policy for cancellation, obviously exercisable only during life, to receive the surrender value, vests the lienor with any right to the proceeds, or any portion thereof, after the death of the insured has definitely terminated the right to receive the surrender value. Cer-

tainly, the liener's rights can rise no higher than those of the licnee.

For the reasons stated, it is respectfully urged, that the decision of the Court in *Behrens* is unsound and without merit.

Since the *Behrens* decision was adopted and followed in *U. S.* vs. *Hoper*, 242 F. (2d) 468, the same arguments apply.

The cross-petitioner, with further reference to the *Behrens* and *Hoper* cases, points out that she relies primarily upon her rights under the contract of insurance as construed by the Courts of New Jersey, and only secondarily upon the statutes, R. S. 17:34-28 and R. S. 17:34-29, *supra*, page

POINT 5.

The cross-petitioner is under no circumstances liable as transferee to the full extent of the net proceeds of the policies.

The District Court entered judgment in the amount of $11,657.30, interpreting *Pearlman* v. *Commissioner*, 153 F. (2d) 560, to hold that the beneficiary was a transferee of the proceeds. The Court below stated that such a conclusion was not warranted by the "Pearlman decision nor is it supported by more recent cases" (Opinion, R. 21). The Court below decided that cross-petitioner was a transferee only of the cash surrender value and directed that judgment be reduced to $3,362.53.

There have been a number of decisions in lower Courts which construed the *Pearlman* case as extending the liability to the full amount of the proceeds. However, all appellate courts agree that the extent of liability is limited to an amount less than the proceeds. The Court of Appeals, 7 Cir., in *United States* v. *New*, 217 F. 2d 166 (1954), reversed the District Court and expressed its rejection of the Government's contention in the following language adopted from *Rowen* v. *Commissioner*, 215 F. 2d at page 644:

> "In no sense were the proceeds ever property of the decedent-taxpayer. Under the policy contracts the decedent never had a right to receive the proceeds. And since at his death, the policies were not payable to his estate, the proceeds of the policies never passed to his estate, and as to the proceeds the beneficiaries did not take as legatees or distributees of his estate." 217 F. 2d 166, 167.

The Court of Appeals, 10 Cir., in a case which did not involve life insurance, *Voss* v. *Wiseman*, 234 F. 2d 237 (1956), held that the liability of a transferee, "where such liability is established", is limited to the amount of the transfer, plus the proper amount of interest applicable to the particular case.

See also *Glenn*, Fraudulent Conveyances and Preferences, *supra*, pages 14, 15.

In no event can the liability exceed either the amount of premiums or the cash surrender value of the policies.

Conclusion.

For the reasons stated, it is respectfully submitted that the cross-petitioner is under no liability to the United States of America, and that the judgment below should be revised accordingly.

MORRIS J. OPPENHEIM,
Counsel for Petitioner,
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1957.

No. 410

MOLLY G. BESS,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

CROSS-PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

MORRIS J. OPPENHEIM,
Attorney for Petitioner,
601 Bangs Avenue,

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Supreme Court of the United States

OCTOBER TERM, 1957.

No. .....

MOLLY G. BESS,

Petitioner,

vs.

UNITED STATES OF AMERICA,

Respondent.

CROSS-PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

TO THE HONORABLE THE CHIEF JUSTICE AND ASSOCIATE JUSTICES OF THE SUPREME COURT OF THE UNITED STATES:

Your petitioner, Molly G. Bess, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Third Circuit entered in the case of *United States of America* v. *Molly G. Bess, Appellant* on the 28th day of March, 1957.

Opinion Below.

The opinion of the District Court is reported in 134 F. Supp. 467. The opinion of the Court of Appeals is reported in 243 F. 2d 675.

Jurisdiction.

The judgment of the Court of Appeals was entered March 28, 1957 (Appendix A, *infra*, p. 14). Rehearing was denied on May 20, 1957 (Appendix A, *infra*, p. 14). On August 9, 1957, by order of Mr. Justice Brennan, the time for petitioning for a writ of certiorari was extended to September 19, 1957. The jurisdiction of this Court is invoked under 28 U. S. C., section 1254.

Questions Presented.

Herman Bess, deceased husband of the petitioner, was indebted for Federal income taxes. The assets of his estate which were subject to claims of creditors were insufficient to pay the income tax debt in full. His life was insured under several life insurance policies over which, at the time of his death, he had the right to change the beneficiary, to borrow against the cash surrender values and the right of assignment. The petitioner, having been named as beneficiary when the policies were taken out, collected the proceeds when the policies matured at death of the insured. Herman Bess was solvent at all times when he paid the insurance premiums. There was no fraud against creditors in taking out the insurance, in naming the petitioner as beneficiary, nor in paying the premiums, nor did any such act render Herman Bess insolvent. The following questions are presented:

1. Whether the petitioner is liable for the payment of the income tax debt of Herman Bess, as a transferee of Herman Bess, to the extent of the cash surrender value of the policies, as was determined below.

Statutes Involved.

New Jersey Revised Statutes, sections 17:34-28 and 17:34-29 are set forth in Appendix B, *infra*, page 15.

Statement.

Petitioner is the widow of Herman Bess who died, a resident of New Jersey, on June 29, 1950 (R. 3a).

The case was tried in the District Court upon a Stipulation of Facts (R. 2a-10a).

At the time of his death there were eight life insurance policies in force on the life of Herman Bess, seven of which were issued in 1934, 1935, 1936 and 1937 (R. 7a, par. 21), the eighth, a group policy, having no cash surrender value was issued in 1950. Prior to his death, Herman Bess had the right to change the beneficiary, borrow against the cash surrender value and the right of assignment. The petitioner was named as beneficiary when the policies were issued and, except for immaterial, temporary changes with respect to two policies, remained as the beneficiary (R. 6a-10a). Petitioner collected the proceeds when the policies matured at insured's death (R. 10a, par. 29). The total cash surrender or loan value of the policies, at date of death, was $3,362.53 (R. 10a, par. 32). Herman Bess paid all of the premiums. He was solvent at all times when such premiums were paid (R. 10a, par. 30).

At the time of his death Herman Bess had personal property and real estate, valued at $55,241.63, held jointly with the petitioner (R. 6a, par. 17). After his death, the Estate of Herman Bess had assets of $6,973.85 and claims of $22,081.06 (R. 5a, par. 11). Included among those claims was that for federal income taxes aggregating $9,428.85 for 1945-1947 inclusive, and $3,990.71 for 1948 and 1949. His estate paid $3,990.71 to the Collector of Internal Rev-

enue in full payment of taxes for 1948 and 1949 and paid $554.28 on account of the taxes due for 1945-1947 inclusive leaving an unpaid balance of $8,874.57 (R. 3a-6a).

The Commissioner of Internal Revenue took no action, at any time, against the petitioner by way of a transferee assessment under Section 311, Internal Revenue Code of 1939 (R. 10a; par. 31).

This action was instituted by complaint filed by United States of America in the United States District Court, District of New Jersey. The complaint alleged that the petitioner was a transferee of property of Herman Bess by virtue of having been beneficiary of his life insurance and thus under a liability, at law or in equity, in respect of the tax owing by said Herman Bess (R. 13a). The trial court, basing its decision on *Pearlman* v. *Commissioner* (C. A. 3d), 153 F. 2d 560, rendered judgment against the petitioner in the amount of $11,657.30 (opinion, R. 11a *et seq.*, Judgment, R. 18a). The Court of Appeals reiterated its ruling in the *Pearlman* case, *supra*, namely, that the question of liability "should be decided on general law as laid down by the Federal courts and not be subject to the limitation in the law of any State," but held that the amount of the liability is limited to the cash surrender value. The Court, accordingly, vacated the judgment of the trial court with a direction to enter judgment in conformity with the opinion (Appendix A, *infra*, p. 14). In footnote No. 3 to its opinion the Court pointed out that no liability attached to the petitioner if New Jersey law were to be applied (Appendix A, *infra*, p. 10).

Reasons for Granting the Writ.

1. Insofar as the decision below holds that New Jersey Revised Statutes, section 17:34-28, and 17:34-29 do not apply and that the liability of a life insurance beneficiary

for the unpaid income taxes of the insured is to be decided by "general law as laid down by the Federal courts" rather than by State law, it is in direct conflict with the recent decision of the Court of Appeals for the Sixth Circuit in *Stern* v. *Commissioner*, 242 F. 2d 322.

In the *Stern* case the Commissioner of Internal Revenue made an assessment of transferee liability, respecting the insured's unpaid income taxes, against the life insurance beneficiary pursuant to Section 311, Internal Revenue Code of 1939. Nevertheless, the Court of Appeals, reversing the Tax Court which had relied on the *Pearlman* case, *supra*, ruled that State law determined the liability, and that the beneficiary was not liable by virtue of Kentucky Revised Statutes (1944, 2d ed.) sections 297.140 and 297.150 which limit recovery from the beneficiary to "the amount of premiums for such insurance paid in fraud of creditors, . . ."

New Jersey Revised Statutes, Sections 17:34-28 and 17:34-29, similarly to the Kentucky statutes, which the Court applied in the *Stern* case, limit the recovery of creditors to "the amount of any premiums for the insurance paid in fraud of creditors. . . .". Since Herman Bess was solvent when he paid the premiums, and premiums were not paid in fraud of creditors, the petitioner is not liable if New Jersey law is applicable.

The Government has filed its petition for writ of certiorari in the *Stern* case, *sub nom. Commissioner of Internal Revenue, Petitioner* v. *Jean F. Stern, Transferee*, October Term 1957, No. 311, asserting the direct conflict as one of the reasons for granting the writ.

2. Petition for writ of certiorari was filed, in this case, on behalf of the United States of America on August 22,

1957. In that petition, review is sought only of the amount of liability. The Government's petition will not present the question presented herein.

Conclusion.

For the reasons stated, this petition for a writ of certiorari should be granted.

Respectfully submitted,

MORRIS J. OPPENHEIM,
Attorney for Petitioner.

August, 1957.

APPENDIX A.

1. Opinion of U. S. Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 12,026

UNITED STATES OF AMERICA

v.

MOLLY G. BESS,

Appellant.

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Argued December 4, 1956

Before BIGGS, Chief Judge, KALODNER, Circuit Judge, and KRAFT, District Judge.

Opinion of the Court.

(Filed March 28, 1957)

By BIGGS, Chief Judge.

The court below gave judgment in favor of the United States against the defendant, Molly G. Bess, widow of Herman Bess, on the theory that under Section 311 of the 1939 Code, 26 USCA (I.R.C. 1939) §311, the defendant was

a transferee of property of a taxpayer, her husband, who owed the government delinquent income taxes.

The facts are not in dispute. The defendant's husband died on June 29, 1950. At the time of his death there were in force eight insurance policies on his life. Seven of the policies were issued during 1934, 1935, 1936, and 1937. The eighth, a group insurance policy with no cash value, was issued June 19, 1950. Herman Bess had the right to change the beneficiary of the policies and also had the right to borrow upon the security of the cash surrender value of the seven policies described first herein. The defendant was named as beneficiary when the policies were issued to Herman Bess, and, except for temporary changes with respect to two policies,[1] the defendant remained the beneficiary. The government and the defendant have assumed, without dispute, that Herman Bess was solvent when the policies were issued, and have stipulated that he was solvent when the premiums were paid. The total cash surrender or loan value of all the policies was $3,362.53 at the time of Bess's death. The defendant received $63,576.95 as the total proceeds of the eight policies.

On July 17, 1952, more than two years after his death, the estate of Herman Bess was adjudged insolvent. Part payment has been made on the claims of the United States for income taxes owed by Herman Bess, but a balance of $8,874.57 remains unpaid. The United States instituted suit against the defendant for that amount plus interest from the date of assessment and was awarded judgment in the sum of $11,657.30. 134 F. Supp. 467 (D.N.J. 1955). Mrs. Bess has appealed.

The statute on which the alleged liability of the defendant is bottomed is Section 311 of the 1939 Internal Revenue

---

[1] In one policy the beneficiary was changed from the defendant to the insured's estate on April 4, 1945, and on the same day the defendant was redesignated as the beneficiary; in another policy the beneficiary was changed from the defendant to the insured's estate on March 23, 1945, and on April 3, 1945 the defendant was redesignated as the beneficiary.

Code, 26 USCA (I.R.C. 1939) §311, set out in the margin.[2] It is the universal view that the statute created no new substantive rights and liabilities and that the only liabilities to be enforced thereunder are those existing in law or in equity when the enforcement proceeding is begun. Pearlman *v.* Commissioner, 153 F. 2d 560, 561-2 (3 Cir. 1946), and Rowen *v.* Commissioner, 215 F. 2d 641, 643 (2 Cir. 1954). Herman Bess was domiciled in New Jersey up to his death. His widow's domicil remains there. In Pearlman *v.* Commissioner, *supra*, at p. 562, we stated that "On principle the question [as to the existence or non-existence of liability on the part of the widow] seems to us clearly to be one to be answered without reference to state law limitations." We also said, since we had before us a husband domiciled in Pennsylvania until his death with his wife's domicil remaining there, that "Whether the reliance is placed on general law as declared by federal courts, or on Pennsylvania law, we think the conclusion of the Tax Court must stand." We may perhaps remark here, without cynicism, that a declaration on principle is not necessarily a declaration of law, but we went on to say that we preferred to rest the decision on the wider ground that since there was a federal tax question to be decided it should be decided on general law as laid down by the Federal courts and not

[2] Section 311 provides in pertinent part: "Transferred assets (a) Method of collection. The amounts of the following liabilities shall, except as hereinafter in this section provided, be assessed, collected, and paid in the same manner and subject to the same provisions and limitations as in the case of a deficiency in a tax imposed by this chapter (including the provisions in case of delinquency in payment after notice and demand, the provisions authorizing distraint and proceedings in court for collection, and the provisions prohibiting claims and suits for refunds):

"(1) Transferees. The liability, at law or in equity, of a transferee of property of a taxpayer, in respect of the tax (including interest, additional amounts, and additions to the tax provided by law) imposed upon the taxpayer by this chapter.

* * *

"(f) Definition of 'transferee'. As used in this section, the term 'transferee' includes heir, legatee, devisee, and distributee."

be subject to the limitation in the law of any State. We adhere to our former ruling but since this case may reach the reviewing Court, other Courts of Appeals having reached the contrary conclusion, Rowen *v.* Commissioner, *supra*, and the authorities cited therein, 215 F. 2d at 648-9, we have set out what we believe to be the status of Mrs. Bess under the law of New Jersey, were that law applicable, in *footnote 3 below*. Cf. Poe *v.* Seaborn, 282 U. S. 101 (1930), and United States *v.* Scott, 167 F. 2d 301 (8 Cir. 1948).

As to the general law as declared by the Federal courts the decision of the Supreme Court in Central Bank of Washington *v.* Hume, 128 U. S. 195 (1888), is illustrative of

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[3] As to the law of New Jersey the applicable sections are New Jersey R.S. 17:34-28 and 17:34-29; NJSA 17:34-28 and NJSA 17:34-29. Section 29 provides that every policy of life insurance made payable to or issued for the benefit of a married woman, or after its issue assigned or in any way made payable to a married woman, whether by her husband or by any other person, shall "inure to her separate use and benefit . . ." according to its terms unless premiums were paid in fraud of creditors as set out in Section 28. There can be no doubt that in the absence of fraud on creditors in the payment of premiums or assignment of the beneficial interest to some person other than to the wife, the wife's interest in the proceeds of a policy has a status described by the law of New Jersey as a "vested interest" and may not be reached by a creditor, even by the United States. Cf. Sullivan *v.* Maroney, 76 N.J.Eq. 104, 109, 73 A. 843, 844 (1909), affirmed 77 N.J.Eq. 565, 78 A. 150 (1910), and Phoenix Mut. Life Ins. Co. *v.* Connelly, 188 F. 2d 462, 464-5 (3 Cir. 1951).

As we have stated the parties have agreed that Herman Bess was solvent when the policies were issued and that he was solvent at all times when premiums were paid. There therefore was no payment of premiums in fraud of creditors and Mrs. Bess was designated as beneficiary at all times save for two small irrelevant periods in respect to only two of the policies. See note 1, *supra*. As to the cash surrender value of the policies, amounting to $3,362.53, though we have found no case in point and none has been cited to us, we are of the opinion that the term "proceeds" as employed in the New Jersey statute means the full amount payable to the beneficiary upon the policy on the death of the insured. It follows therefore that under the law of New Jersey Mrs. Bess may retain the full proceeds of the policies in the instant case without liability for the claim asserted by the United States against her husband for unpaid taxes.

features of it. The decision holds, *inter alia*, that it is the general rule that a policy and the money to become due under it, belong, the moment the policy is issued to the person named in it as the beneficiary. The policies of insurance in the *Hume* case quite possibly did not provide that the insured could change the beneficiary but this feature, as we have indicated, is irrelevant here. Hume was admittedly insolvent at the time that the insurance was effected and it was argued that the policies were within the provisions of 13 Elizabeth, c. 5. The Supreme Court was of the view that the statute of 13 Elizabeth governed and held *inter alia* that Hume's creditors were not entitled to recover the premiums paid by him on life insurance policies issued for the benefit of his wife and children. The statute of 13 Elizabeth was designed to prevent conveyances which defeated or delayed creditors. It declares, in substance, that every conveyance made to the end, purpose, and intent to delay, hinder, or defraud creditors and others of their just and lawful actions shall be void, with the proviso that nothing therein contained shall extend to defeat any estate or interest made on good consideration and bona fide to any person having, at the time, no notice of such fraud. 24 Am. Jur., Fraudulent Conveyances § 4, p. 163. See Annotation, 31 A.L.R. 51. The statute of 13 Elizabeth is generally acknowledged to be the principal source of judicial decision as to when a conveyance is fraudulent. *Id.* at p. 164. The statute is declaratory of the existing principles of the common law. *Ibid.* We believe that the governing principles of the general law are as set out in this paragraph.

Coming now to our decision in the Pearlman case we find that the court below interpreted our ruling as requiring it to decide that the proceeds of the policies in the case at bar were transferred to Mrs. Bess[4] on her husband's death. We think that such a conclusion was not warranted by our

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[4] We conclude this because, while the proceeds of the policies amounted to $63,5[illegible].95, and the judgment in favor of the United States to $11,657.30, the amount of the judgment far exceeded the cash surrender value of the policies which, as we have stated in this opinion, was $3,362.53.

Pearlman decision[5] nor is it supported by more recent cases.[6] The proceeds of the policies—putting cash surrender values to one side for the time being—were not the property of Herman Bess as required by Section 311(a)(1). He never possessed the right to receive the proceeds and therefor he could not transfer them. Moreover, as we have stated, Bess was solvent when the policies were issued and solvent at all times when premiums were paid. In the Pearlman case, while Pearlman was solvent when the policies were issued and when some of the premiums were paid, after he became insolvent and up to the time of his death he continued to pay the premiums on the policies. In Pearlman we went no further than the Tax Court which held that the beneficiaries of the policies were transferees as to the cash surrender value of the policies. In the case at bar Mrs. Bess cannot be found to be a transferee of the *proceeds* of the policies under the general law as we have set it out.

The cash surrender values of the policies in the instant case present a different issue. Bess was adjudicated insolvent more than two years after his death but the account filed by Mrs. Bess as executrix makes it clear that he also was insolvent at the time of death. At the time of his death, as we have stated, the policies possessed a cash surrender or loan value of $3,362.53. He therefore possessed just prior to his death, a chose in action in the amount stated which he could have collected from the insurance companies in accordance with the terms of the policies. The Supreme Court in the Hume case, *supra*, seemed to recognize the payment of premiums as transfers and the incidence of the payments of premiums therefore timed the transfers here. By the terms of the policies in the Hume case noth-

[5] The facts of the case as found by the Tax Court in 4 T.C. 34 (1944) disclose that the cash surrender values of the pertinent policies totaled $51,541 and that the tax liability was $25,713.57. See Rowen *v.* Commissioner, 215 F. 2d 641, 645 (2 Cir. 1954) on this point.

[6] See United States *v.* New, 217 F. 2d 166, 167 (7 Cir. 1954), and Rowen *v.* Commissioner, 215 F. 2d 641, 644 (2 Cir. 1954).

ing passed at the time of Hume's death. So was it here. It is therefore not realistic here, as the court pointed out in *Rowen* v. *Commissioner*, *supra*, 215 F. 2d at p. 647, in a like situation, to view Bess's death as wiping out the loan or surrender values. Bess's death was merely a condition on the occurrence of which the loan or surrender values of the policies no longer were payable to him but became merged in the larger values which the insurance companies were obligated to pay to Mrs. Bess. The loan or surrender values were then an item of property and Mrs. Bess was a transferee of them within the meaning of Section 311(a)(1). It follows that the United States is entitled to recover the amount of the loan or surrender values from her.

Other points raised by the parties do not require discussion.

The judgment of the court below will be vacated with the direction to enter judgment for the United States in conformity with this opinion.

A true Copy:

Teste:

Clerk of the United States Court of Appeals
for the Third Circuit.

2. Judgment of the U. S. Court of Appeals.

[Caption Omitted.]

(Filed March 28, 1957.)

On Appeal from the United States District Court for the District of New Jersey.

Present:

Biggs, Chief Judge, Kalodner, Circuit Judge, and Kraft, District Judge.

Judgment.

This cause came on to be heard on the record from the United States District Court for the District of New Jersey and was argued by counsel

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court in this case be, and the same is hereby vacated, with direction to enter judgment for the United States of America in conformity with the opinion of this Court.

March 28, 1957

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3. Judgment of U. S. Court of Appeals Denying Petition for Rehearing.

[Caption Omitted.]

(Filed May 20, 1957.)

Present:

Biggs, Chief Judge, and Kalodner, Circuit Judge, and Kraft, District Judge.

After due consideration the petition for rehearing in the above-entitled case is hereby denied.

By the Court

Biggs
Chief Judge

APPENDIX B.

New Jersey R. S. 17:34-28. Beneficiary's Right to Proceeds.

When a policy of insurance is effected by any person on his own life, or on another life in favor of a person other than himself having an insurable interest therein, the lawful beneficiary thereof, other than himself or his legal representative, shall be entitled to its proceeds, against the creditors and representatives of the person effecting it. The person to whom a policy of life insurance is made payable may maintain an action thereon in his own name. Subject to the statute of limitations, the amount of any premiums for the insurance paid in fraud of creditors, with interest thereon, shall, however, inure to their benefit from the proceeds of the policy, but the company issuing the policy shall be discharged of all liability thereon by payment of its proceeds in accordance with its terms, unless, before the payment, the company shall have written notice by or in behalf of some creditor, with specification of the amount claimed, claiming to recover for certain premiums paid in fraud of creditors.

Source. L. 1902, c. 134, Sect. 38, p. 422 (C. S., p. 2850, Sect. 38).

New Jersey R. S. 17:34-29. Policies to Inure to Benefit of Married Woman.

Every policy of life insurance made payable to or for the benefit of a married woman, or after its issue assigned, transferred or in any way made payable to a married woman, or to any person in trust for her or for her benefit, whether procured by herself, her husband or by another person, and whether the assignment or transfer is made by her husband or by another person, shall inure to her separate use and benefit, and to that of her children, according to the terms and provisions of the policy or assignment, subject to the foregoing provisions relating to premiums paid in fraud of creditors.

Source. L. 1902, c. 134, Sect. 39, p. 422 (C. S., p. 2850, Sect. 39).

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No. 410

In the Supreme Court of the United States

October Term, 1957

MOLLY G. BESS, PETITIONER

v.

UNITED STATES OF AMERICA

On Cross-Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

MEMORANDUM FOR THE UNITED STATES

J. LEE RANKIN,
Solicitor General,
Department of Justice,
Washington 25, D.C.

In the Supreme Court of the United States

October Term, 1957

No. 410

MOLLY G. BESS, PETITIONER

v.

UNITED STATES OF AMERICA

On Cross-Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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MEMORANDUM FOR THE UNITED STATES

The issue presented by the cross-petition is whether the beneficiary of life insurance policies of a decedent who retained, during his life, the right to draw cash surrender values and the right to change the beneficiary, and who died insolvent while owing delinquent income taxes to the Government, is liable as a transferee to the extent of the cash surrender values. Petitioner correctly states that as to this issue the decision of the Court of Appeals for the Third Circuit in the instant case is in direct conflict with the decision of the Court of Appeals for the Sixth Circuit in the case of *Stern* v. *Commissioner*, 242 F. 2d 322, and that the Government has petitioned for a writ

of certiorari in the *Stern* case (No. 311, this Term), asserting the conflict.

The Government's petition in the instant case, No. 395, filed August 22, 1957, raises the issue of the beneficiary's liability, in these same circumstances, to the full extent of the proceeds of the insurance policies. The two issues are closely related and, we submit, should be heard together by this Court. Accordingly, although we believe that the decision below, insofar as it upholds the Commissioner, is correct, the Government does not oppose the cross-petition for a writ of certiorari.

Respectfully submitted,

J. LEE RANKIN,
Solicitor General

September, 1957.

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